REGISTERED NUMBER: 05167021

Southern Gas Networks Plc

Strategic Report, Directors' Report and

Financial Statements for the Year Ended 31 March 2019

Contents of the Financial Statements
for the Year Ended 31 March 2019

Company Information
for the Year Ended 31 March 2019

DIRECTORS:	Gregor Alexander (Chairman) Charlotte Brunning Natalie Flageul Paul Jeffery Guy Lambert Robert McDonald John McManus Charles Thomazi (Alternate) Ines Grund (Alternate) Nicholas Robin Salmon Laura Sandys Peter McCosker (Alternate) Michael McNicholas
SECRETARY:	Nicola Shand
REGISTERED OFFICE:	St Lawrence House Station Approach Horley Surrey RH6 9HJ
REGISTERED NUMBER:	05167021
AUDITOR:	KPMG LLP, Statutory Auditor Chartered Accountants 15 Canada Square London E14 5GL

Strategic Report
for the Year Ended 31 March 2019

This strategic report sets out the main trends and factors underlying the development and performance of the Company during the year ended 31 March 2019 as well as those matters which are likely to affect its future development and performance.

THE BUSINESS, ITS OBJECTIVES AND STRATEGY
The Company operates the regulated gas transportation business for the South and South East of England gas distribution network, one of eight regional gas distribution networks in the United Kingdom. Its gas distribution network comprises approximately 49,000 kilometres of gas mains delivering natural gas to approximately 4.0 million domestic, commercial and industrial customers. The network stretches from Milton Keynes in the north, to Dover in the east and Lyme Regis in the west, including London boroughs to the south of the River Thames.

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks Limited ("**SGN**"), which is registered at St. Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ. SGN is owned by a consortium made up of SSE plc, Borealis Infrastructure Europe (UK) Limited, which is indirectly wholly owned by OMERS Administration Corporation, OTPPB Investments (U.K.) Limited, which is owned by Ontario Teachers' Pension Plan Board and Blue Spyder B 2016 Limited, which is owned by Abu Dhabi Investment Authority. References to the "**Group**" throughout this Report mean SGN and its subsidiaries (including the Company).

The Company's business is regulated by the Office of Gas and Electricity Markets ("Ofgem").

Objectives and Strategy
The Company's principal objectives are to deliver natural gas safely, reliably and efficiently across the gas distribution network and to provide the highest standard of service to our stakeholders, whilst delivering value to our shareholders. Its strategy therefore places the highest emphasis on ensuring activities are carried out safely and that the networks operate in a reliable and efficient manner, so that benchmarks and regulatory targets can be exceeded to the benefit of all its stakeholders.

The Company's overall financial objective is to focus on operational efficiency and the efficient delivery of capital and replacement expenditure programmes. Therefore, financial objectives are set to ensure the regulatory targets are achieved or outperformed.

The Company's financing objective is to ensure an efficient capital structure that mitigates interest rate risk through maintaining a minimum of 75% of debt at either fixed rates of interest or index linked.

External and regulatory environment
The management and operation of the Company's gas transportation assets are subject to a series of legislative requirements to ensure that assets are managed and operated in a safe and reliable manner. The Company must also ensure that arrangements are in place to respond to emergency situations and to ensure hazardous work is carried out safely and with minimum disruption.

The primary legislation controlling the Company's activities as a gas transporter is the Gas Act 1986 (as amended). Under the Gas Act, the Company holds a licence that allows it to operate the gas distribution network it owns. The Company is regulated by Ofgem, which has established price control mechanisms that govern the amount of revenue that can be earned by regulated businesses. Ofgem assesses the revenue and investment plans of the Company to determine an efficient level of expenditure and the quality of service requirements for the network are also taken into account. A cost of capital for the required investment in the networks is also determined.

The Company is also subject to safety legislation which is enforced by the Health and Safety Executive ("**HSE**") in the UK. The Group's processes and procedures are covered in a safety case which has been accepted by the HSE.

Factors affecting the business

The Company's principal activity is the operation of a highly complex gas infrastructure network. As a consequence, there are a number of factors that may influence the development and performance of the Company and the financial returns that can be achieved. The principal factors that influence the Company are as follows:

- **Regulatory price controls**

  As outlined above, the prices that can be charged for the use of the Company's networks are determined in accordance with regulator approved price controls. The outcome of the eight-year review baselined the revenues that will be obtained over the price control period. In addition, targeted incentive schemes were introduced by the regulator whereby the Company can earn additional revenues by outperforming the targets, or alternatively penalised if the Company does not meet them.

  Additionally, the regulatory price controls include an allowed rate of return for the investment the Company makes in the network. The level of the allowed rate of return determines the extent to which investment to increase the quality and capacity of the network is economically viable.

- **Safety and reliability of the networks**

  The Company's ability to operate the networks safely and reliably is of the highest importance. Its performance in these areas affects the costs it incurs and the overall financial performance.

- **Efficiency**

  The Company's objective is to ensure that gas is delivered as efficiently as possible through its network. This allows the Company to limit price increases and improve its own financial performance.

- **Interest rates**

  The costs of financing our operations are affected by changes in interest rates as some of the Company's borrowings are held at floating rates. Exposure to changes in interest rates are hedged by holding both fixed rate and index linked borrowings and by holding derivative financial instruments (interest rate swaps) where necessary to achieve the desired profile of interest rate risk.

PRINCIPAL RISKS AND UNCERTAINTIES

As well as the opportunities the Company has to grow and develop its business, certain risks and uncertainties are faced in achieving its objectives. The principal risks and uncertainties identified are as follows:

Description and Impact of Risk	Mitigation
Health and safety: Failures in the design or implementation of our safety, health and environmental management system may result in unsafe behaviour and working practices resulting in injuries or fatalities involving employees, contractors or members of the public; asset damage or loss; harm to the environment and prosecution under relevant legislation.	Safety is the first of our core Company values with a continued focus across all assets and operations. The Safety, Health and Environmental Advisory Committee of the Board and the Engineering Safety Committee (ESC) are responsible for ensuring our safety, health and environmental policy is developed and adhered to. Compliance is supported by independent inspections and an audit programme with reporting of the issues to ESC. Our ongoing safety initiative included rolling out behavioural based intervention focusing on employee behaviour and risk awareness. Updating of safety performance indicators focussing on key operational performance. There is continued engagement with different levels e.g. relevant authorities and industry peers.
Regulatory and legislative compliance: Failure to comply with regulatory requirements could result in prosecution, damage to our reputation and financial penalties.	Governance and compliance frameworks are in place to deal with issues and developments arising from this price control. We have experienced regulation, finance and legal teams which manage compliance requirements and engage with all levels of Ofgem and government. The delivery of regulatory outputs is measured and monitored on a regular basis. Information requirements to regulators, government, customers, and the public were all addressed in a timely manner during the year. Compliance with material changes were dealt with on a risk-based approach e.g. GDPR.
Political and policy risk: Regulatory, legislative or political reform could have an adverse impact on our business model. The Labour party has pledged to bring utilities back into public ownership. The future of the gas network is threatened if the energy mix scenarios rule out a role for gas by switching to other heat systems.	We have policy and public affairs specialists who engage openly and constructively with legislators, officials and other policy makers on all aspects of energy and related environmental policies. We have a proactive public affairs campaign with relevant stakeholders to highlight the long-term value of our networks and benefits to the customers. We are piloting projects to evidence future use of gas and working with others to test potential decarbonisation pathways.

	Our reviews of the UK's decision to leave the EU do not indicate any material issues for our model but our assessments are ongoing and mitigations for the supply chain are in place.
Asset management systems: Failures in the design or implementation of our asset management systems including health, physical security and integrity may result in a major incident leading to loss of life; adverse impact on the environment; loss of assets; prosecution under relevant legislation and; failure to meet our licence conditions.	We have a comprehensive asset management system and are accredited by Lloyds Register with the internationally recognised IS0 55000. We have a strong framework of engineering governance and risk management to ensure all assets have a strategic plan through their lifecycle and are tracked through a number of committees reporting into the Engineering and Safety Committee. A number of audits and inspections are undertaken annually. Developments during the year included: a damage prevention group set up to oversee improved procedures & learning from high pressure incidents, completion of a major review of accident hazards and a refresh of process safety indicators. There is an on-going security improvement programme for designated sites based on Centre for the Protection of National Infrastructure's (CPNI) good practice. Crisis management and business continuity plans are regularly evaluated.
Cyber security risk and IT service failure: Failures to implement appropriate security management of IT systems and physical assets could result in unauthorised access to our IT systems; unauthorized or fraudulent disclosure of sensitive information; vulnerability to external cyber-attack.	We continue to manage a long-term information security programme intended to reduce the risk that cyber related attack could harm business resilience. We conduct regular internal and external penetration and vulnerability tests of our network with government approved security partners to review our security position. There are ongoing improvements to reduce cyber risk. Industry leading threat intelligence and response capability has been adopted to reduce cyber risk. A Senior Business Continuity Manager has been appointed to continue developments in business continuity plans and crisis management processes.
Finance risk: Failure to finance our obligations and new projects due to economic climate, lack of availability of finance, and a failure to set appropriate targets and sufficient management information, could lead to inability to deliver expected financial returns.	The funding position is regularly reported to the Board and the Regulator, giving comfort that funding is available under all conditions. Financing activities and relationships are maintained and developed with a diversified source of funding providers. There is continuous monitoring of the markets, including foreign exchange, interest rate and inflation rate movements. Tracking performance against allowances and monitoring key performance indicators is carried out as part of the business planning performance.

Maintaining a competent, productive and talented workforce: Failure to maintain a sufficiently competent, diverse and productive workforce with effective relationships and sufficient talent may result in resource/workload mismatches; failure to meet licence, regulatory or legislative requirements; or take advantage of business opportunities.	Workforce planning and recruitment programme is regularly reviewed by the executive and the board and supported by external benchmarking and compliance audits. Also, ensuring that critical skills and knowledge are retained in the business. To mitigate against an ageing workforce, talent management processes including succession planning are being enhanced to improve identification and retention of key talent. Employer brand and remuneration packages are being reviewed to attract good candidates and also enhance inclusivity and diversity within the company.
RIIO-GD2 Price Control: The risk profile associated with the next price control RII0-GD2 (from 2021-2022) exposes us to greater uncertainty which could lead to lower returns compared to current price control.	We are maintaining regular dialogue with the Regulator and actively participating in the Working Groups to influence the development of the price control. We are seeking stakeholder and customer support and alignment with the business plan submission. There is alignment of ongoing projects and business processes with the needs of the next business plan.

The Board reviews the principal risks and uncertainties facing the business and considers the risk management processes in place, which are designed to safeguard assets and to manage, rather than eliminate, material risks to the achievement of business objectives. These reviews recognise that any such process can provide only reasonable, and not absolute, assurance against material misstatement or loss. Further details of the processes the Board has in place are also set out in the Corporate Governance Statement, in the Directors' Report.

Stakeholders

The Company has a range of external stakeholders including gas consumers, employees, suppliers and contractors, its regulator Ofgem, the HSE and local governments and communities. The Company adopts an open and constructive approach, both in terms of the way it operates, the services it provides and the impact that its activities have on each of its stakeholders. The Company encourages and enables its employees to be active citizens in the communities in which they live and work, through schemes which support staff who are either raising money for, or giving their time to, UK charities, local community or youth sports groups. The Company matches eligible fund raising by individual members of staff.

Key performance indicators

The Company measures the achievement of its objectives through the use of quantitative assessments and, where quantitative measures are less relevant, through the use of qualitative assessments. The principal key performance indicators ("KPIs") which are used to assess whether principal operating objectives have been achieved are set out below:

Key performance indicator	Description	Year ended 31 March 2019	Year ended 31 March 2018
Operating profit	Profit before financing costs and taxation	**£366m**	£316m
Capital expenditure	Additions to fixed assets	**£76m**	£90m
Replacement expenditure	Replacement expenditure is capitalised under FRS 102. It represents the cost of renewing sections of gas network with modern polyethylene pipes to improve future safety and reliability. The sections replaced include mains and smaller diameter service pipes, which connect customers and mains.	**£215m**	£196m
Debt to RAV ratio [1]	The Company's debt to RAV ratio	**72.9%**	73.2%
Employee lost time incidents	Incidents resulting in employees taking time off work (per 100,000 hours worked)	**0.10** [4]	0.12 [4]
Customer satisfaction - planned interruptions	Results from customer satisfaction surveys(10 = very satisfied)	**8.8** [2]	8.7 [2]
Customer satisfaction - unplanned interruptions	Results from customer satisfaction surveys (10 = very satisfied)	**9.4** [3]	9.4 [3]
Escapes attendance	Proportion of uncontrolled escapes attended in one hour - percentage (target 97%)	**98.7** [4]	98.8 [4]
Customer complaint volume reduction	This represents the year on year reduction in complaints expressed as a percentage. Complaint means any expression of dissatisfaction related to any areas of our operation.	**40%** [4]	4% [4]

[1] "RAV" is defined as Ofgem Regulatory Asset Value plus adjustments relating to the sharing of out/under performance against allowances. Debt for the purposes of the Debt to RAV ratio excludes liabilities arising from derivative financial instruments. The percentages stated are as at 31 March.

[2] Based on customer satisfaction survey reports obtained for the nine-month period ended 31 December 2018 and 2017 for the Group.

[3] Based on customer satisfaction survey reports obtained for the nine-month period ended 31 December 2018 and 2017 for the Group.

[4] This KPI is measured for the Group, and accordingly the data presented is that for the Group.

Resources
The Company's principal resources are its assets and its people.

The Company's distribution network comprises approximately 49,000 kilometres of gas mains, together with associated services, plant and machinery and storage facilities.

The Company had 556 full time equivalent employees at 31 March 2019 (2018: 606). It places considerable value on the involvement of employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Company during the year. It continues to invest in the development and training of its people in order to ensure both individual developmental needs and business skill requirements are met.

FINANCIAL REVIEW
The Company sets out below its financial review for the year ended 31 March 2019. The comparative figures presented are for the year ended 31 March 2018, as reported in the audited financial statements, unless otherwise stated.

Turnover for the year ended 31 March 2019 was £797m (2018: £746m) and has increased predominantly as a result of inflation and increased incentive income from regulatory returns, this is offset by a reduction in customer tarrifs; this remains a substantial reduction from revenue due to outperformance of the allowances set by Ofgem. The majority of turnover was earned from charges made for the provision of gas transportation capacity as well as revenue based upon gas volumes transported in the year.

Profit for the year before taxation amounted to £242m (2018: £198m) and profit for the year after taxation amounted to £198m (2018: £160m).

Operating profit increased to £366m (2018: £316m) driven by the above-mentioned increase in turnover.

The Company paid dividends of £68m (2018: £1,047m) during the year. Note that £930m of dividends paid in 2018 were non-cash and were due to the repayment of amounts owed from the Company's parent, Scotia Gas Networks Limited, the dividends have been offset against the historic intercompany balance.

Capital expenditure (excluding replacement expenditure) during the year amounted to £76m (2018: £90m). Capital expenditure is incurred to ensure that the networks continue to operate at minimum agreed pressures and that sufficient storage capacity is available to meet instances of peak demand, as well as when new connections or increased capacity are added to the networks.

In the year ended 31 March 2019 the Company sold surplus land and property sites to other SGN Group companies, these are referred to as the SGN Place entities. These companies will focus on redevelopment of the surplus sites.

Treasury policies and capital structure
The Company's operations are financed by a combination of equity and retained profits, bank borrowings and long-term bonds. The Company's funding and liquidity are managed within a framework of policies and guidelines authorised by the Board of Directors. Further details are set out in the Directors' Report.

As a matter of policy, a minimum of 75% of debt is maintained at either fixed rates of interest or index linked. This policy is kept under review from time to time. Interest rate swaps are used, where necessary, in order to achieve this desired profile.

As at 31 March 2019, the Company's total senior debt (before issue costs) amounted to £2,818m (2018: £2,768m) and the debt to RAV ratio was 72.9% (2018: 73.2%). Of the total long-term borrowings at 31 March 2019, after taking into account the effect of interest rate swaps, 89.0% were at either fixed rates of interest or were index linked (2018: 84.4%).

Pension commitments
A large proportion of the Company's employees are members of the Scotia Gas Networks Pension Scheme which provides final salary defined benefits for members.

The Company accounts for any pension asset or liability in accordance with FRS 102. The net pension asset as at 31 March 2019 was £120m (2018: £117m). Following the actuarial valuation carried out by the scheme's actuary as at 31 March 2015, annual special pension contributions remain at a similar level for the Group at £23m (Company's share: £14m). These additional contributions will be paid annually until 31 March 2027 to repair the actuarial deficit in the defined benefit pension scheme. The Company's normal contributions remain at 37.3%. The Company's actuary will undertake a triennial review during 2018/19 to update the actuarial deficit for recent changes in external and market conditions.

Liquidity and cash flows
Liquidity is maintained through a mixture of long term borrowings and short-term liquid funds in order that there are sufficient funds available for the Company's current and planned operations. Committed facilities are in place in order to provide funding for future capital and replacement expenditure as well as to provide sufficient available facilities to meet the seasonal working capital requirements of the Company. The revolving credit facility totalled £360m for the Group and is in place until March 2023; as at 31 March 2019 £350m is undrawn. At 31 March 2019 the Company's committed undrawn revolving credit facility amounted to £230m (2018: £240m).

Counterparty credit risk
The Company transacts with banks for the provision of interest rate and currency hedging transactions. The Company takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy; however, it recognises that at times the market conditions for banks can be unusually tight. At the year end the Company had £35m payable relating to financial instruments with bank counterparties.

Dividend policy
The Company's policy is to distribute to its shareholders any available surplus funds, after taking into account the cash requirements needed to continue to invest in the business and the Company's level of gearing, and subject to the availability of distributable profits.

Accounting policies
The Company's accounting policies are set out in note 1 to the financial statements. These accounting policies have been applied consistently during the year and in the preceding year.

OPERATIONAL REVIEW
Safety
Injury performance
The Company's overriding goal is to distribute gas safely and reliably and to ensure a safe workplace for its workforce with everyone striving towards eliminating injuries. This year the lost time injury performance rate decreased slightly to 0.10 injuries per 100,000 hours (2018: 0.12).

Board responsibility
The Board has a Safety, Health and Environmental Advisory Committee that is responsible for monitoring health and safety performance and ensuring the health and safety policy statement is adhered to. The Committee provides the Board with reports on any key areas identified and further details on the Committee are set out in the Corporate Governance Statement, in the Directors' Report.

Gas mains replacement programme
The Company replaces the iron pipes with modern polyethylene pipes to improve the safety of the existing network. Replacement expenditure, primarily of iron pipes, increased to £215m (2018: £196m).

Gas escapes standards of service
The Company's engineers respond to reports of suspected gas leaks 24 hours a day, 365 days a year, regardless of from whom people buy their gas. Its engineers aim to attend all uncontrolled gas escapes within one hour and all controlled gas escapes within two hours. A controlled gas escape is one where the person reporting it has confirmed that the gas emergency control valve serving the premises has been turned off and the smell of gas has gone. An uncontrolled gas escape covers all others. The Company's engineers exceeded Ofgem targets by attending over 98% of uncontrolled gas escapes within one hour.

Gas networks' regulation
Gas network companies are subject to economic regulation through Price Control Reviews set by industry regulator Ofgem. The current eight-year price control (RIIO) commenced in April 2013 and runs through until March 2021.

Revenues are earned through charges levied on network users, to cover costs and earn a return on the network company's regulated assets. Ofgem also has incentives in the price control to encourage greater efficiency, innovation and delivery of an enhanced standard of service for customers.

With six years of RIIO complete the Company has performed well on outputs set by the regulator, including those for innovation, customer satisfaction and stakeholder engagement.

Further details
Further details on the long-term development plans of the Company can be found in the long-term development statement (published in accordance with Special Condition D3 of the Gas Transporter Licences) and available on the Company's website - www.sgn.co.uk. The long-term development plans set out the forecast gas demand over the ten-year period and outlines the capital investment plan that is required to ensure the continued operation of the network in accordance with the Company's licence conditions.

APPROVED BY THE BOARD AND SIGNED ON ITS BEHALF BY:

Gregor Alexander (Chairman) - Director

16 July 2019

Directors' Report
for the Year Ended 31 March 2019

The Directors present their report and the audited financial statements for the year ended 31 March 2019.

PRINCIPAL ACTIVITY
The Company's principal activity is the development, administration, maintenance and operation of the South and South East of England gas distribution system and the supply of gas transportation services. It will continue in this activity for the foreseeable future.

DIVIDENDS
The Company paid an interim dividend of £68m (2018: £1,047m of which £117m is a cash dividend). The remaining £930m of the dividend in 2018 is due to the repayment of amounts owed from the Company's parent, Scotia Gas Networks Ltd, the dividends have been offset against the historic intercompany balance. The Directors do not recommend the payment of any final dividend for the year (2018: £nil).

FUTURE DEVELOPMENTS
Details of future developments can be found in the strategic report.

EVENTS SINCE THE END OF THE YEAR
Information relating to events since the end of the year is given in the notes to the financial statements.

DIRECTORS
The directors shown below have held office during the whole of the period from 1 April 2018 to the date of this report.

Gregor Alexander (Chairman)
Natalie Flageul
Paul Jeffery
Guy Lambert
Robert McDonald
John McManus
Charles Thomazi (Alternate)

Other changes in directors holding office are as follows:

Charlotte Brunning - appointed 2 May 2018
Andrew Jonathan Mark Taylor - resigned 14 March 2019
Graham Gerald Juggins - resigned 6 September 2018
Mariana Popa (Alternate) - appointed 15 May 2018
Ines Grund (Alternate) - appointed 18 July 2018
Neil Fleming - resigned 2 May 2018
Kenton Edward Bradbury (Alternate) - resigned 14 September 2018
Nicholas Robin Salmon - appointed 14 March 2019
Laura Sandys - appointed 1 October 2018

Peter McCosker (Alternate) and Michael McNicholas were appointed as directors after 31 March 2019 but prior to the date of this report.

Alejandro Lopez Delgado and Mariana Popa (Alternate) ceased to be directors after 31 March 2019 but prior to the date of this report.

DIRECTORS' INSURANCE AND INDEMNITIES
The Directors of the Company have the benefit of the indemnity provisions in the Company's Articles of Association. The Directors have been granted a qualifying third-party indemnity provision which was in force throughout the year. In addition, SGN has purchased and maintained throughout the year Directors' and officers' liability insurance in respect of itself, the Group, the Directors and other senior executives of the Group.

REVIEW OF BUSINESS

The review of business for the year, including an analysis using key performance indicators, together with a description of the principal risks and uncertainties facing the Company are set out in the strategic report.

FINANCIAL RISK MANAGEMENT

The Company's funding, liquidity and exposure to interest rate and foreign exchange risks are managed within a framework of policies and guidelines authorised by the Board of Directors.

Interest rate risk

The Company has interest bearing liabilities, and as a matter of policy a minimum of 75% of debt is maintained at either fixed rates of interest or index linked. This policy is kept under review from time to time. The Company uses interest rate swaps, where necessary, in order to achieve this desired profile.

Liquidity risk

The Company maintains a mixture of long-term funding and short-term liquid funds in order to ensure that there are sufficient funds available for the Company's current and planned operations.

Foreign exchange risk

All of the Company's borrowings are currently denominated in Pound Sterling, so there is no foreign exchange risk. However, in accordance with its policy, should the Group decide to raise finance in currency other than Pound Sterling, cross currency swaps would be used to fully hedge the borrowings into Pound Sterling.

Credit risk

The Company transacts with banks for the provision of interest rate and currency hedging transactions. The Company takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy; however, it recognises that at times the market conditions for banks can be unusually tight. In respect of short-term cash management, counterparties are subject to review and approval according to defined criteria.

Trade receivables predominantly relate to transportation income from gas shippers. Credit risk arising from the Company's regulated business is managed in accordance with industry standards as set out by the Unified Network Code.

The Company contracts with shippers having investment grade ratings only, or where suitable collateral or cash prepayments are made.

Pricing risk

The Company's gas transportation charges are subject to price control formulae set within the regulatory regime. The Company's maximum allowed revenue in a given price period is dependent upon a number of factors that are not known in advance and therefore the maximum allowed annual revenue is not known until the end of the relevant period.

However, transportation tariffs are set on a prospective basis based upon expected transportation volumes, so actual revenue received or receivable in any one year may differ from the maximum allowed revenue. Where revenues received or receivable differ from the maximum allowed annual revenue, adjustments are made to future prices to reflect this over or under recovery.

EMPLOYEES
The Company places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the Company. Participation by employees generally is encouraged through team meetings, briefings, adigital app and an intranet site. The CEO and other senior executives regularly communicate with employees through these channels and employee representatives are consulted regularly on a wide range of matters affecting their current and future interests.

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure their employment within the Company continues and that appropriate training and development is arranged. It is the policy of the Company that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

GOING CONCERN
The Company's financial position, cash flows, liquidity position and borrowing facilities together with the factors likely to affect its future performance and the principal risks and uncertainties are set out in the strategic report. The financial risk management objectives and risk exposures are set out above.

As stated in the strategic report the Company operates the regulated gas distribution networks in the South and South East of England. The revenue of the Company is regulated by Ofgem through established price control mechanisms based on the distribution network capacity. The Company has considerable financial resources together with committed financing facilities to finance the current and future operations.

The Company's forecasts and projections, including performing scenario testing and sensitivity analysis, show the Company should be able to operate within the level of its current facilities. As a consequence, the Directors believe that the Company is well placed to manage its business risks successfully despite the current uncertain economic outlook. After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

ENVIRONMENT AND SUSTAINABILITY
In April 2019 we decided to retire our Greenplan Strategy and focus on a wider reaching strategy to take us up to 2021. This interim strategy adds aspects such as renewable energy production, green energy purchase and the number of electric vehicles available to our staff. To tie up with GD2 we are looking to start our full Sustainability strategy in 2021 which will look at global and local aspects such as the United Nations Sustainable Development Goals.

Greenplan results
Greenplan has run since 2013 and has done what it intended, raised the profile of Environmental targets and led to great reductions in several areas, with others still needing improvement.

Natural gas shrinkage is a major part of our busines carbon footprint and accounts for 95.4% of the total. Shrinkage is made up of leakage from the network, own use of gas and theft of gas. Reducing natural gas emissions from Shrinkage has the largest effect on reducing our carbon footprint when compared with the other elements. We have achieved a 18.8% reduction in natural gas shrinkage since 2013/14 which equates to 184,647 tonnes of CO_2 equivalent. The reductions are largely achieved through our Mains Replacement Programme, Optimising and driving down operating pressures, Gas conditioning, Asset Investment and Innovation.

Since 2013/14 we have reduced our carbon emissions from Business Travel by 3.6%. After rolling out Skype for Business and working to reduce the carbon intensity of our vehicle fleet we are hoping to see further reductions.

Behind shrinkage reductions, Waste to Landfill has been one of our biggest Greenplan successes with landfilled waste falling 99% to 0.1%. We are now looking at ways to close the loop further and increase reuse and recycling rates.

PE Pipe is one of our most commonly used resources. As part of Greenplan we had targeted to improve the efficiency which we buy and lay pipe. Since 2013 we have improved our PE pipe efficiency by 18%.

As a result of these works we produce a large amount of scrap PE which we can't reuse. In 2018/19 PE scrap volumes were 275 tonnes, this gets recycled into low pressure pipe, drainage pipe and other useful items such as ground matting. We are working with our PE suppliers and recycling company to further improve efficiency and packaging.

Since 2013 our gas and electricity usage in offices, depots and metered operational sites showed a small increase of 4% as our property portfolio changed. We recognise we need to do more to improve our energy efficiency so have completed renewable energy feasibility studies at our highest usage sites. These studies show us where is best to invest to increase renewable energy production and reduce our reliance our grid electricity.

Our overall Business Carbon Footprint is shown in the Table below:

	2018/19		2017/18		Annual Movement Decrease/ (increase)	
	Tonnes of CO_2e	Tonnes of CO_2e per £1m turnover	Tonnes of CO_2e	Tonnes of CO_2e per £1m turnover	Tonnes of CO_2e	Tonnes of CO_2e per £1m turnover
Scope 1						
Energy consumption (excluding electricity)	192	0.24	210	0.28	18	0.04
Transport (direct commercial vehicles and business miles)	9,765	12.27	9,727	13.04	(38)	0.77
Scope 2						
Electricity consumption	2,557	3.21	2,214	2.97	(343)	(0.24)
Scope 3						
Rail, air and ferry travel	12,531	15.74	13,981	18.74	1,450	3.00
Total (excluding shrinkage)	**25,045**	**31.46**	**26,132**	**35.02**	**1,087**	**3.56**
Shrinkage	86,085	736.29	608,104	815.04	22,019	78.76
Total carbon emissions	**11,130**	**767.75**	**634,236**	**850.07**	**23,106**	**82.32**

Data has not been independently verified

CORPORATE GOVERNANCE STATEMENT

The Board of Directors is the principal decision making forum for the Company and is committed to the highest standards of corporate governance. The Board believes that strong governance improves the performance of the Company and enhances shareholder value. This report sets out the key governance principles and practices of the Company.

The Company, not having listed equity shares, is not subject to the UK Financial Reporting Council's UK Corporate Governance Code [1] (the "Governance Code"), and the Board of Directors has decided not to voluntarily apply the Governance Code as they do not consider all the guidance to be applicable to the Company. However, for the purposes of this statement, the Directors have elected to provide additional disclosure in relation to governance to provide a clearer understanding of the Company.

Board of Directors

The Board of Directors is comprised entirely of non-executive Directors and is the principal decision-making forum for the Company. Directors are nominated to the Board in accordance with the terms of the Shareholders' and Governance Agreement.

The Board is collectively responsible to the Company's shareholders for the long-term success of the Company and for its overall strategic direction, its values and its governance. It provides the leadership necessary for the Company to meet its business objectives whilst ensuring that a sound system of internal control and risk management is in place. The powers and the duties of the Directors are determined by legislation and by the Company's Articles of Association. The Board has also adopted a formal schedule of matters detailing key aspects of the Company's affairs reserved to it for decision. Furthermore, the Board has established four standing committees and one non-standing committee with specific responsibilities to ensure focused and effective leadership. Details of the committees are set out below.

The Board meets regularly and has held eight meetings during the year.

Board Constitution and Appointments

The Board of Directors consists of seven non-executive Directors in addition to the non-executive Chairman, as well as two additional independent non-executive Directors.

The non-executive Directors scrutinise, measure and review the performance of management; constructively challenge and assist in the development of strategy; review the Company financial information and ensure systems of internal control and risk management are appropriate and effective.

Chairman

Gregor Alexander was re-appointed as Chairman on 18 July 2018.

Chief Executive Officer and Chief Financial Officer

Below the Board, executive responsibility rests with John Morea, Chief Executive Officer ("CEO") and Mick Carmedy, Chief Financial Officer ("CFO"). They are supported by an executive committee which meets on a monthly basis and is responsible for managing the day-to-day operations of the Company.

[1] The UK Corporate Governance Code was issued in April 2016 (replacing the Combined Code on Corporate Governance), applies to financial years beginning on or after 17 June 2016 and is available on the Financial Reporting Council's website (www.frc.org.uk).

Timeliness and quality of Board information
The Board has sought to ensure that Directors are properly briefed on issues arising at board meetings. This is done by establishing procedures for distributing board papers one week in advance of meetings; considering the adequacy of the information provided before making decisions; adjourning meetings or deferring decisions when Directors have concerns about the information available to them and making the Company Secretary responsible to the Board for the timeliness and quality of information.

All Directors have access to the advice and services of the Company Secretary.

Conflicts of interest
With effect from 1 October 2008, the Companies Act 2006 has introduced a statutory duty on Directors to avoid conflicts of interest. During the year, the Company Secretary reviewed all of the Directors' reported actual and potential conflicts of interest and the Board then considered and recorded each Director's reported actual and potential conflicts of interest.

The Board has put into place a procedure to consider any future actual or potential conflicts of interest that the Directors may have and will review the position regularly.

Board Committees
In order to provide effective and focused leadership, the Board of Scotia Gas Networks Limited has established four standing committees and one non-standing committee with specific responsibilities. These are the Audit Committee, the Safety, Health and Environmental Advisory Committee, the People and Reward Committee, the Finance Committee, and the GD2 Committee (non-standing). These committees act for and on behalf of the wider group, in particular Southern Gas Networks Plc and Scotland Gas Networks Plc.

Each Committee's performance, constitution and terms of reference are reviewed annually to ensure that they are operating effectively.

The Company Secretary acts as secretary for each committee and further details are set out below.

Audit Committee
The current members of the Audit Committee are John McManus (Committee Chairman), Paul Jeffery, Gregor Alexander, Charlotte Brunning and Guy Lambert.

The principal responsibilities of the Audit Committee are as follows:-
- Ensuring that the Company's financial reports represent an accurate, clear and balanced assessment of the Company's position and prospects;
- Ensuring the economy, efficiency and effectiveness of the Company's operations and internal controls, the reliability and integrity of information and accounting systems, and the implementation of established policies and procedures;
- Monitoring and reviewing the Company's internal audit function; and
- Maintaining a close relationship with the Company's external auditor and reviewing the effectiveness of the external audit process.

As part of its activities, the Audit Committee also reviews and approves key regulatory filings prior to their issue to Ofgem.

The Chairman of the Audit Committee reports to the Board of Directors following each committee meeting on the main areas and subjects the Committee has reviewed such as risk management, internal control, internal audit reports and any issues arising from its review of the financial statements.

The Board considers that the membership of the Audit Committee as a whole has sufficient recent and relevant financial experience to discharge its functions. The Committee met three times during the year.

Safety, Health and Environmental Advisory Committee
The current members of the Safety, Health and Environmental Advisory Committee are Natalie Flageul (Committee Chair), Andrew Jonathan Mark Taylor (resigned March 2019), Laura Sandys (replacing Graham Juggins), John McManus (replacing Alejandro Lopez Delgado), Guy Lambert, John Morea (Chief Executive Officer) and Paul Denniff (Network Director).

The principal responsibilities of the Safety, Health and Environmental Advisory Committee are as follows:
- Ensuring that the health and safety policy statement and environmental policy statement remain fit for purpose and are being adhered to;
- Reviewing and monitoring the safety, health and environmental strategy and action plan, which shall be designed to eliminate, reduce or otherwise control personal and process related data;
- Reviewing and monitoring the safety, health and environmental compliance and assurance plan (and liaising with the internal auditors in relation thereto);
- Setting health and safety, and environmental targets to improve the Company's performance;
- Monitoring health and safety and environmental performance against planned targets and identified key improvement areas by means of appropriate leading and lagging key performance indicators; and
- Encouraging greater awareness of the importance of health, safety and the environment and higher achievement in performance in these areas.

The Chairman of the Safety, Health and Environmental Advisory Committee reports to the Board of Directors following each committee meeting on the main areas and subjects the Committee has reviewed. Four meetings were held during the year.

People and Reward Committee
The current members of the People and Reward Committee are Andrew Jonathan Mark Taylor (resigned March 2019), Alejandro Lopez Delgado (replacing Andrew Jonathan Mark Taylor as Committee Chairman) and Gregor Alexander.

The principal responsibilities of the People and Reward Committee are as follows:
- To determine and agree with the Board of Directors the Company's framework or broad policy for executive and senior management remuneration. The Committee has delegated authority for setting the remuneration of the CEO, CFO and their direct reports; and
- To review the ongoing appropriateness and relevance of the remuneration policy.

The Chair of the People and Reward Committee reports to the Board of Directors following each Committee meeting on the remuneration matters which the Committee has reviewed. Three meetings were held during the year.

Finance Committee
The current members of the Finance Committee are Charlotte Brunning (Committee Chair), Guy Lambert, Gregor Alexander, Alejandro Lopez Delgado and Paul Jeffery.

The principal responsibility of the Finance Committee is to authorise specific transactions of the Company where it has been provided delegated authority by the Board of Directors to do so. The members of the Finance Committee report to the Board of Directors following each Committee meeting on the matters which the Committee has reviewed. Six meetings were held during the year.

GD2 Committee
The current members of the GD2 Committee are Rob McDonald (Committee Chairman), Charlotte Brunning, and Alejandro Lopez Delgado.

The primary responsibility of the GD2 Board Committee is to provide leadership and challenge on the RIIO-2 process and business plan that will be developed for the RIIO-2 period that will enter into force from April 2021. The Committee is a leadership and challenge group, with recommendations to be reported back to the Board of Directors. The committee meets alongside the main board with additional meetings as necessary.

Board and Committee Performance Evaluations
During the year, the Board has undertaken a comprehensive evaluation of its own performance and that of its four standing committees, one non-standing committee and individual Directors. This was conducted internally using detailed questionnaires which the Chairman then discussed with each Director and the Company Secretary. The Board has considered and discussed the outcomes of the evaluations and is satisfied that it is operating well and focused on the correct strategic issues. The Directors continue to review the Board's performance and that of its five Committees and individual Directors on an annual basis.

Attendance at Board and Board Committee meetings
The attendance of the Board of Directors and the Board Committees during the year is as set out below.

	Board meetings		**Audit Committee meetings**		**People and Reward Committee meetings**	
	Attended	Possible	Attended	Possible	Attended	Possible
Gregor Alexander	8	8	3	3	3	3
Robert McDonald	7	8	-	-	-	-
Natalie Flageul	8	8	-	-	-	-
John McManus*	7	8	3	3	2	2
Alejandro Lopez Delgado*	8	8	-	-	1	1
Andrew Jonathan Mark Taylor**	6	8	-	-	3	3
Charlotte Brunning	8	8	3	3	-	-
Guy Lambert	3	8	2	3	-	-
Paul Jeffery	8	8	3	3	-	-
Graham Juggins**	3	3	-	-	-	-
Laura Sandys***	5	5	-	-	-	-
Nicholas Salmon***	1	1	-	-	-	-
Mariana Popa****	5	5	-	-	-	-

	Safety, Health and Environment Committee meetings		**Finance Committee meetings**		**GD2 Committee meetings**	
	Attended	Possible	Attended	Possible	Attended	Possible
Gregor Alexander	-	-	7	7	-	-
Robert McDonald	-	-	-	-	7	7
Natalie Flageul	4	4	-	-	-	-
John McManus*	2	2	-	-	-	-
Alejandro Lopez Delgado*	2	2	7	7	7	7
Andrew Jonathan Mark Taylor**	-	-	-	-	-	-
Charlotte Brunning	-	-	7	7	7	7
Guy Lambert	1	4	4	7	-	-
Paul Jeffery	-	-	7	7	-	-
Graham Juggins**	2	2	-	-	-	-
Laura Sandys***	2	2	-	-	-	-
Nicholas Salmon***	-	-	-	-	-	-
Mariana Popa****	-	-	1	1	7	7

* John McManus became a member of the Safety, Health & Environmental Advisory Committee in January 2019. Alejandro Lopez Delgado became a member of the People and Reward Committee in March 2019.
** Andrew Jonathan Mark Taylor resigned on 14 March 2019. Graham Juggins resigned on 06 September 2018.
*** Laura Sandy was appointed on 01 October 2018. Nicholas Salmon was appointed on 14 March 2019.
**** Attended as an Alternate Director for Blue Spyder B 2016 Limited.

Internal Controls in relation to the Company's financial reporting process
The Board of Directors is ultimately responsible for the Company's internal control systems and risk management. The Company's system of internal control and embedded risk management, which has been in place throughout the year, helps to safeguard the assets and is designed to manage, rather than eliminate, material risks to the achievement of the business objectives. The Board recognises that these systems can provide only reasonable, and not absolute, assurance against material misstatement or loss.

Accordingly, the Directors have regard to what controls, in their judgement, are appropriate to the business, to the materiality of the risks inherent in the business, and to relative costs and benefits of implementing specific controls. Internal control is maintained through an organisation structure with clearly defined responsibilities, authority levels and lines of reporting, the appointment of suitably qualified staff in specialised business areas, and continuing investment in high quality information systems. These methods of control are subject to periodic review as to their implementation and continued suitability.

There were no changes in the Company's internal controls over financial reporting during the year covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Internal audit
The Board of Directors has established the scope of the internal audit function which is responsible for reviewing the effectiveness of the Company's systems of internal control and reports to the Audit Committee of the Board. The internal audit manager reports to the Audit Committee on the audit programme, progress against the programme and any follow-up actions on a bi-monthly basis.

Directors' and Senior Executives' Biographies and Responsibilities as at 31 March 2019

Gregor Alexander, Chairman
Gregor joined the Board of the Company at its inception and was appointed Chairman in July 2011. He is Finance Director of SSE plc and previously worked with the accountancy firm Arthur Andersen. He is a member of the Audit Committee, the People and Reward Committee, and the Finance Committee.

Robert McDonald, Director
Robert joined the Board of the Company in July 2006. He is Managing Director SSEN Transmission and has previously worked with the industry's regulatory body. Rob is the Chairman of the GD2 Committee.

Natalie Flageul, Director
Natalie joined the Board of the Company in September 2011. She is Director of Customer Experience at SSE plc and previously oversaw the transformation to nationwide coverage in preparation for Smart Meter deployment. She is the Chair of the Safety, Health and Environmental Advisory Committee.

Charlotte Brunning, Director
Charlotte joined the Board in May 2018. She is a member of the EMEA Infrastructure and Natural Resources team and had been with Ontario Teachers' since 2015. She has been involved in a number of direct investments, including London City Airport and SGN Smart. Charlotte holds a B.Sc. from the London School of Economics and an MBA from the London Business School. She is the Chair of the Finance Committee and a member of the Audit Committee and GD2 Committee.

John McManus, Director
John joined the Board of the Company in March 2012. He is Senior Advisor to OMERS Infrastructure in asset management, assessment of investment opportunities, relationship development and mentorship. John is the Chairman of the Audit Committee and a member of the Safety, Health and Environmental Advisory Committee.

Guy Lambert, Director
Guy joined the Board in October 2016. He joined the Abu Dhabi Investment Authority (ADIA) in 2008 and currently serves as the Head of Utilities. He is responsible for sourcing and executing new investments in the utilities sector and overseeing the existing utilities portfolio. Guy is a member of the Audit Committee, the Finance Committee and the Safety, Health and Environmental Advisory Committee.

Alejandro Lopez Delgado, Director
Alejandro joined the Board in November 2015. He is a Director at OMERS Infrastructure, where he is responsible for the origination, acquisition and management of infrastructure investments, with a focus in Europe. He is a member of the People and Reward Committee, the GD2 Committee and the Finance Committee.

Nick Salmon, Director
Nick Salmon joined the Board in March 2019 as a Teachers' nominee. He is also currently Chairman of South East Water Ltd and Senior Independent Director of Elementis plc. Previously he was a Non-executive director of United Utilities plc and Interserve plc and CEO of Cookson Group plc and Babcock International Group plc.

Mariana Popa, Alternate Director
Mariana joined the Board in May 2018 and is a Senior Investment Manager at ADIA. She attends Board meetings as a substitute to Guy Lambert.

Ines Grund, Alternate Director
Ines joined the Board in July 2018 and is a director at OMERS Infrastructure, responsible for the active management of infrastructure investments. She attends Board meetings as a substitute to Alejandro Lopez Delgado.

Charles Thomazi, Alternate Director
Charles joined the board in October 2017 and leads the EMEA Infrastructure team in Teachers' Infrastructure Group. He attends board meetings as a substitute to Charlotte Brunning.

Paul Jeffery, Non-executive Director
Paul joined the Board in January 2014. Previously he ran the European Power, Utility and Infrastructure Investment Banking Sector team for Barclays. Paul is also a non-executive Director of UK Power Networks. Paul is a member of the Audit Committee and the Finance Committee.

Laura Sandys, Non-executive Director
Laura joined the board in October 2018. She was a member of the Energy and Climate Change Select Committee and co-founder of POWERful Women which promotes women's role in the energy sector. She has been appointed a member of the Government's CCUS Council and is a Member of Imperial College's Centre for Carbon Capture and Storage Advisory Group.

John Morea, Chief Executive Officer
John joined the Company in May 2005 from SSE plc. He has over 30 years' experience in the energy industry. John is a companion of the Institute of Gas Engineers and Managers, a member of the Institute of Engineering and Technology and holds an MBA.

Mick Carmedy, Chief Financial Officer
Mick joined the Company in January 2018. Mick was CFO of Southern Water, the regulated water business, for five years prior to joining. Mick has also worked at United Utilities Water and Thames Water in a wide variety of roles.

Nicola Shand, Company Secretary
Nicola joined the Board as Company Secretary in July 2011. Nicola is Director of Legal and Compliance and is responsible to the Board for compliance with Board procedures and for advising and keeping the Board up to date on all corporate governance developments.

AUDITOR
Each of the Directors at the date of this report confirms that:
1) So far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
2) The Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provision of section 418 of the Companies Act 2006.

BY ORDER OF THE BOARD:

Nicola Shand - Secretary

16 July 2019

Directors' Responsibilities Statement
for the Year Ended 31 March 2019

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they are required to prepare the financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

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 its profit or loss for that period. In preparing the financial statements, the directors are required to:
- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate Company or to cease operations, or have no realistic alternative but to do so.

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 its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Strategic Report, Directors' Report, and Corporate Governance Statement that complies with that law and those regulations.

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

Responsibility statement of the directors in respect of the annual financial report

We confirm that to the best of our knowledge:
- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the directors' report includes a fair review of the development and performance of the business and the position of the issuer, together with a description of the principal risks and uncertainties that they face.

1 Our opinion is unmodified

We have audited the financial statements of Southern Gas Networks plc ("the Company") for the year ended 31 March 2019 which comprise the Profit and Loss Account, Statement of Comprehensive Income, Balance sheet, Statement of Changes in Equity, Cash Flow Statement and the related notes, including the accounting policies in note 1.

In our opinion the financial statements:

- give a true and fair view of the state of Company's affairs as at 31 March 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were first appointed as auditor by the directors on 18 July 2017. The period of total uninterrupted engagement is for the 2 financial years ended 31 March 2019. We have fulfilled our ethical responsibilities under, and we remain independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

2 Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
Retirement benefit obligation (£548m (2018: £504m)) Refer to page 42 (accounting policy) and page 55 (financial disclosures). Risk direction: (unchanged)	The Company operates a defined benefit pension scheme. Significant estimates are made in valuing the Company's pension obligation. Small changes in the assumptions and estimates used to value the Company's pension obligation (before deducting scheme assets), including in particular the discount rate, the inflation assumptions, the cash commutation assumptions and mortality assumptions, would have a significant effect on the financial position of the Company. Where there has been a change in actuary performing the valuation, different assumptions or methodology may be used in the calculation of the Company's pension obligation. There is also risk around completeness and accuracy of the pensions related disclosures in the financial statements.	Our procedures included: **Control design and implementation:** We evaluated the design and implementation of controls around the valuation assumptions for the pension liability. **Benchmarking Assumptions:** With the assistance of our own actuarial specialists, we challenged key assumptions applied, including discount rate and inflation rate, and performed a comparison of key assumptions against market data. **Assessing actuaries' credentials:** We assessed the competence, independence and integrity of the Company's actuarial expert. **Assessing transparency:** We have considered the adequacy of the Company's disclosures in respect of the sensitivity of the defined benefit obligation to key assumptions. Our results: We found the estimate of the retirement benefit obligation to be acceptable (2018: acceptable)

	The risk	Our response
Cost classification between Capex, Repex and Opex (£278m (2018: 267m) plant and machinery additions) Refer to page 37 (accounting policy) and page 49 (financial disclosures). Risk direction: (unchanged)	Costs are classified between capital expenditure, replacement expenditure, and operating expenditure. Specifically for the plant and machinery asset category, given the size and nature of expenditure within the business, judgement is required to ensure appropriate allocation of costs between capital, replacement and operating expenditure. There is a risk that the allocation around classification of these costs is incorrect, with expenditure misstated between the profit and loss account and balance sheet. The incentive to capitalise more costs to increase profit exists, though the incentive for management bias is reduced because of the Totex regime within GD-1 that the Company operates under.	Our procedures included: **Control design and operation:** We evaluated the controls around the authorisation of capital and replacement expenditure, including their operating effectiveness. We evaluated general IT controls, including access controls, to ensure that the ability to make changes to system configuration and project classification was restricted to appropriate individuals. **Accounting analysis:** We assessed whether the Company's accounting policies for capitalisation are in accordance with relevant accounting standards, including the capitalisation criteria. **Tests of details:** With the assistance of our data specialist team, we interrogated the integrity of the Company's overhead allocation model. We also assessed the appropriateness of the cost classification for a sample of projects, including by inspecting supporting documentation, such as approved budget reports completed for each project, to gain an understanding of the nature and type of costs incurred and to assess this against the criteria for capitalisation or expensing. Our results: We found the cost classification between Capex, Repex and Opex to be acceptable (2018: acceptable)

We continue to perform procedures over environmental provisions. However, the vast majority of sites have been subject to a recent third party inspection, reducing the risk of error. Therefore, we have not assessed this as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

We continue to perform procedures over financial instruments. However, whilst the Company uses derivatives, the valuation is based upon observable prices. Therefore, we have not assessed this as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

3 Our application of materiality and an overview of the scope of our audit

Materiality for the statutory financial statements as a whole was set at £12.0 million (2018: £9.8 million), determined with reference to a benchmark of profit before tax of £242.0 million (2018: £197.8 million), of which it represents 5% (2018: 5%).

We reported to management any corrected or uncorrected identified misstatements exceeding £600,000 (2018: £490,000), in addition to other identified misstatements that warranted reporting on qualitative grounds.
The audit was performed using the materiality levels set out above, covering 100% of the profit before taxation and total assets held.

4 We have nothing to report on going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease its operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Company will continue in operation.

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Company's business model, including the impact of Brexit, and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period. We evaluated those risks and concluded that they were not significant enough to require us to perform additional audit procedures Based on this work, we are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least a year from the date of approval of the financial statements.

We have nothing to report in these respects, and we did not identify going concern as a key audit matter.

5 We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and directors' report
Based solely on our work on the other information:
- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

We are also required to report to you if a corporate governance statement has not been prepared by the company. We have nothing to report in these respects.

6 We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements 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.

We have nothing to report in these respects.

7 Respective responsibilities

Directors' responsibilities
As explained more fully in their statement set out on page 23, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.
A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities - ability to detect
We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience and through discussion with the directors and other management (as required by auditing standards) and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably.

The company is subject to laws and regulations that directly affect the financial statements including Ofgem regulations, financial reporting legislation (including related companies legislation), distributable profits legislation, environmental legislation, taxation legislation, and pension legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Whilst the company is subject to many other laws and regulations, we did not identify any others where the consequences of non-compliance alone could have a material effect on amounts or disclosures in the financial statements.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8 The purpose of our audit work and to whom we owe our responsibilities

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.

Ian Griffiths (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

17 July 2019

Profit and Loss Account
for the Year Ended 31 March 2019

	Notes	2019 £m	2018 £m
TURNOVER		797	746
Net operating costs		(431)	(430)
OPERATING PROFIT		366	316
Interest receivable and similar income	4	6	4
Interest payable and similar charges	5	(130)	(122)
PROFIT BEFORE TAXATION	6	242	198
Tax on profit	7	(44)	(38)
PROFIT FOR THE FINANCIAL YEAR		198	160

The notes on pages 36 to 60 form part of these financial statements

Statement of Comprehensive Income for the Year Ended 31 March 2019

	Notes	2019 £m	2018 £m
PROFIT FOR THE YEAR		198	160
OTHER COMPREHENSIVE (LOSS)/INCOME			
Gains arising on cash flow hedges		1	1
Remeasurement net defined benefit asset		(9)	106
Income tax relating to components of other comprehensive (loss)/income		2	(18)
OTHER COMPREHENSIVE (LOSS)/INCOME FOR THE YEAR, NET OF INCOME TAX		(6)	89
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		192	249

The notes on pages 36 to 60 form part of these financial statements

Balance Sheet
31 March 2019

	Notes	2019 £m	2018 £m
FIXED ASSETS			
Intangible assets	9	241	251
Tangible assets	10	4,412	4,237
		4,653	4,488
CURRENT ASSETS			
Debtors	11	79	74
Short term deposits	12	-	266
Cash at bank		10	10
		89	350
CREDITORS			
Amounts falling due within one year	13	(243)	(625)
NET CURRENT LIABILITIES		(154)	(275)
TOTAL ASSETS LESS CURRENT LIABILITIES		4,499	4,213
CREDITORS			
Amounts falling due after more than one year	14	(2,834)	(2,675)
PROVISIONS FOR LIABILITIES	17	(536)	(560)
ACCRUALS AND DEFERRED INCOME	18	(229)	(199)
PENSION ASSET	21	120	117
NET ASSETS		1,020	896
CAPITAL AND RESERVES			
Called up share capital	19	160	160
Hedge reserves	20	-	(1)
Profit and loss account	20	860	737
SHAREHOLDERS' FUNDS		1,020	896

The financial statements were approved by the Board of Directors on 16 July 2019 and were signed on its behalf by:

Gregor Alexander (Chairman) - Director

The notes on pages 36 to 60 form part of these financial statements

Statement of Changes in Equity
for the Year Ended 31 March 2019

	Called up share capital £m	Profit and loss account £m	Hedge reserves £m	Total equity £m
Balance at 1 April 2017	160	1,536	(2)	1,694
Changes in equity				
Profit for the year	-	160	-	160
Other comprehensive income	-	88	1	89
Total comprehensive income	-	248	1	249
Dividends	-	(1,047)	-	(1,047)
Total transactions with owners, recognised directly in equity	-	(1,047)	-	(1,047)
Balance at 31 March 2018	160	737	(1)	896
Changes in equity				
Profit for the year	-	198	-	198
Other comprehensive income	-	(7)	1	(6)
Total comprehensive income	-	191	1	192
Dividends	-	(68)	-	(68)
Total transactions with owners, recognised directly in equity	-	(68)	-	(68)
Balance at 31 March 2019	160	860	-	1,020

The notes on pages 36 to 60 form part of these financial statements

Cash Flow Statement
for the Year Ended 31 March 2019

	Notes	2019 £m	2018 £m
Cash flows from operating activities			
Cash generated from operations	1	455	1,344
Interest paid		(110)	(101)
Tax paid		(49)	(56)
Net cash from operating activities		296	1,187
Cash flows from investing activities			
Purchase of intangible fixed assets		(5)	(6)
Purchase of tangible fixed assets		(291)	(277)
Sale of tangible fixed assets		8	5
Customer contributions received		35	17
Interest received		6	-
Net cash from investing activities		(247)	(261)
Cash flows from financing activities			
Issue of debt		160	400
Loan repayments in year		(400)	-
Payments for financial instruments		(7)	(7)
Increase/decrease in short term deposits		266	(266)
Equity dividends paid		(68)	(1,047)
Net cash from financing activities		(49)	(920)
Increase in cash and cash equivalents		-	6
Cash and cash equivalents at beginning of year	2	10	4
Cash and cash equivalents at end of year	2	10	10

The notes on pages 36 to 60 form part of these financial statements

Notes to the Cash Flow Statement
for the Year Ended 31 March 2019

1. **RECONCILIATION OF PROFIT BEFORE TAXATION TO CASH GENERATED FROM OPERATIONS**

	2019	2018
	£m	£m
Profit before taxation	242	198
Depreciation charges	109	104
(Profit)/loss on disposal of fixed assets	(1)	1
Amortisation of deferred income	(5)	(5)
Amortisation charges	15	14
Finance costs	130	122
Finance income	(6)	(4)
	484	430
(Increase)/decrease in trade and other debtors	(5)	913
(Decrease)/increase in trade and other creditors	(24)	1
Cash generated from operations	455	1,344

2. **CASH AND CASH EQUIVALENTS**

The amounts disclosed on the Cash Flow Statement in respect of cash and cash equivalents are in respect of these Balance Sheet amounts:

Year ended 31 March 2019

	31.3.19	1.4.18
	£m	£m
Cash and cash equivalents	10	10

Year ended 31 March 2018

	31.3.18	1.4.17
	£m	£m
Cash and cash equivalents	10	7
Bank overdrafts	-	(3)
	10	4

1. **ACCOUNTING POLICIES**

General information and basis of preparation
Southern Gas Networks Plc is a private limited Company incorporated in the United Kingdom under the Companies Act 2006. The address of the registered office is St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ. The Company's principal activity is the development, administration, maintenance and operation of the South and South East of England gas distribution system and the supply of gas transportation services.

The financial statements have been prepared under the historical cost convention, modified to include certain items at fair value, and in accordance with Financial Reporting Standard 102 - 'The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland' (FRS 102) issued by the Financial Reporting Council. There were no material departures from that standard.

The functional currency of Southern Gas Networks Plc is considered to be pounds sterling because that is the currency of the primary economic environment in which the Company operates. Amounts are expressed in millions of pounds except where noted otherwise.

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks Limited and the financial statements of the Company are included in the consolidated financial statements of Scotia Gas Networks Limited which can be obtained from the address above. Consequently, the Company has taken exemptions available under FRS 102 in relation to financial instruments, presentation of a cash flow statement, intra-group transactions and remuneration of key management personnel.

Going concern
After reviewing the Company's forecasts and projections, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. The current liabilities position has arisen due to £400m of debt repayments falling due in 2018/19, new finance will be raised in the coming financial year to meet these repayments. The Directors do not foresee any reason why these funds will not be raised to meet existing liabilities due to the Company's good standing in the debt capital markets. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements. See also director's report for discussion on going concern.

Turnover
Turnover is stated net of value added tax and is attributable to the continuing activity of transportation of natural gas and the provision of related services. Turnover is recognised to the extent that there is a right to consideration and is recorded at the value of the consideration due. Turnover includes an assessment of transportation services supplied to customers between the date of the last meter reading and the year end.

Where revenues received or receivable differ from the amount permitted by regulatory agreements, adjustments will be made to future prices to reflect this over or under recovery.

Intangible assets - goodwill
Goodwill arising on the acquisition of businesses, representing any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight line basis over its useful economic life, which is estimated to be 50 years. Provision is made for any impairment, and it is tested on an annual basis at each balance sheet date.

1. **ACCOUNTING POLICIES - continued**

Intangible assets - software
Software assets are included at cost, net of amortisation and any provision for impairment. Amortisation is provided in equal annual instalments over a period of 3 to 10 years, which is their estimated useful economic life.

Tangible fixed assets
Tangible fixed assets are stated at cost, net of depreciation and any provision for impairment. In accordance with Ofgem guidance for gas transportation licensees, costs include an element of capitalised overheads which are, as far as reasonably practicable, allocated in accordance with the activities which lead to the generation of the assets. These costs are directly attributable to the associated assets. Depreciation is provided on all tangible fixed assets, other than freehold land, at rates calculated to write off the cost or valuation, less estimated residual value, of each asset on a straight-line basis over its expected useful life, as follows:

Freehold buildings:	Up to 50 years
Leasehold land and buildings:	Over the shorter of lease term and 50 years
Plant and machinery:	
-Mains and services:	55 to 65 years
-Regulating equipment:	30 to 50 years
-Gas storage:	40 years
-Motor vehicles and office equipment:	3 to 10 years

Site remediation costs are depreciated over the life of the asset.

Replacement expenditure is capitalised within mains and services and depreciated accordingly above.

Residual value represents the estimated amount which would currently be obtained from disposal of an asset, after deducting estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Fixed Asset Investments
Fixed asset investments are stated at cost less a provision for any impairment in value. Costs of the investments include all costs directly related to the acquisition of the investments.

1. **ACCOUNTING POLICIES - continued**

Financial instruments
FRS 102 sections 11 and 12 give an accounting policy choice for financial instruments. The Company has chosen to apply the recognition and measurement provisions of IAS 39 (as adopted for use in the EU) and the disclosure requirements of FRS 102 in respect of financial instruments.

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

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

The Company's funding, liquidity and exposure to interest rate risks are managed within a framework of policies and guidelines authorised by the Board of Directors. In accordance with these policies financial derivative instruments are used to manage interest rate and currency exposure.

Where appropriate these instruments are recorded at fair value and accounted for as described below.

i. Effective interest method
The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or where appropriate, a shorter period.

Income and expense is recognised on an effective interest basis for debt instruments other than those financial assets designated as at 'fair value through profit or loss' (FVTPL).

ii. Financial Assets
Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned and are initially measured at fair value, plus transaction costs, except for those financial assets classified as FVTPL, which are initially measured at fair value.

Financial assets at the balance sheet date are classified into the following specified categories: financial assets at FVTPL, 'held-to-maturity' investments, 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

iii. Impairment of financial assets
For financial assets carried at amortised cost, the amount of an impairment is 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.

For financial assets carried at cost less impairment, the impairment loss is the difference between the asset's carrying amount and the best estimate of the amount that would be received for the asset if it were to be sold at the reporting date.

1. **ACCOUNTING POLICIES - continued**

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade debtors.

Where indicators exist for a decrease in impairment loss, and the decrease can be related objectively to an event occurring after the impairment was recognised, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired financial asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised.

iv. Derecognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

v. Trade debtors

Trade debtors are initially recognised at fair value. The carrying amount is reduced through the use of provision. Appropriate provision for estimated irrecoverable amounts are recognised where the estimated cash flows are less than the carrying amount. Subsequent recoveries of amounts previously written off are credited against the provision account. Changes in the carrying amount of the provision account are recognised in profit or loss.

vi. Cash

Cash comprises cash on hand and demand deposits, which are those deposits, which are repayable on demand and available within 24 hours (one day) without penalty.

vii. Financial liabilities

Financial liabilities are classified as either financial liabilities at 'FVTPL' or 'other financial liabilities'.

viii. Financial liabilities at FVTPL

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

A financial liability is classified as held for trading if:
- It has been incurred principally for the purpose of disposal in the near future; or
- It is a part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or
- It is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:
- Such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- The financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy and information about the Company is provided internally on that basis; or
- It forms part of a contract containing one or more embedded derivatives and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL

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

1. **ACCOUNTING POLICIES - continued**

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

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

xi. Derivative financial instruments and hedge accounting
The Company uses interest rate swaps and foreign exchange forward contracts to hedge interest rate and foreign currency risk arising on debt instruments. On inception of the hedge relationship the Company documents the relationships between the hedged item and the hedging instrument along with the risk management objectives and its strategy for undertaking various transactions. Furthermore, at inception of the hedge and on an ongoing basis the Company documents whether the hedging relationship is highly effective.

Changes in fair value of derivatives that are designated and are effective as hedges of future cash flows are recognised directly in equity within the hedge reserve. The ineffective portion of the hedge is recognised through the profit and loss account.

Changes in the fair value of derivatives that do not qualify for hedge accounting are recognised in the profit and loss account as they arise.

Hedge accounting is discontinued when the hedge instrument expires or is terminated.

Financial assets and financial liabilities are offset where they are settled net as a matter of practice and there is legal right to offset.

Taxation
Current tax, including UK corporation tax and foreign 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 arises from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that, 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.

1. **ACCOUNTING POLICIES - continued**

Deferred tax is measured using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date that are expected to apply to the reversal of the timing difference.

Where items recognised in other comprehensive income or equity are chargeable to or deductible for tax purposes, the resulting current or deferred tax expense or income is presented in the same component of comprehensive income or equity as the transaction or other event that resulted in the tax expense or income.

Current tax assets and liabilities are offset only when there is a legally enforceable right to set off the amounts and the Company intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Deferred tax assets and liabilities are offset only if: a) the Company has a legally enforceable right to set off current tax assets against current tax liabilities; and b) the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Foreign currency

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are reported at the rates of exchange prevailing at that date.

Other exchange differences are recognised in profit or loss in the year in which they arise except for exchange differences on transactions entered into to hedge certain foreign currency risks (see below), and exchange differences arising on gains or losses on non-monetary items which are recognised in other comprehensive income.

1. **ACCOUNTING POLICIES - continued**

Employee benefits

i. Defined benefit pension scheme

The Company participates in a group wide defined benefit pension plan administered by the ultimate parent undertaking, Scotia Gas Networks Limited. The net defined benefit cost of the plan is charged and accounted for based on the proportionate number of members relating to the Company. The contributions payable by the Company is determined on the same basis as the charging policy above.

For defined benefit schemes the amounts charged to operating profit are the costs arising from employee services rendered during the year and the cost of plan introductions, benefit changes, settlements and curtailments. They are included as part of staff costs. The net interest cost on the net defined benefit liability is charged to profit or loss and included within finance costs. Remeasurement comprising actuarial gains and losses and the return on scheme assets (excluding amounts included in net interest on the net defined benefit liability) are recognised immediately in other comprehensive income.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the Company, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit credit method. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date.

A surplus was recognised due to change in actuarial assumptions. It is probable that the surplus recognised will result in reduced amount of future contributions to the scheme or in the form of refund from the scheme. Since the amount recognised is within the cap allowed under regulation, management deem the recognition of surplus appropriate.

ii. Defined contribution pension scheme

For defined contribution schemes the amount charged to the profit and loss account in respect of pension costs and other retirement benefits is the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

Impairment of non-financial assets

Assets, other than those measured at fair value, are assessed for indicators of impairment at each balance sheet date. If there is objective evidence of impairment, an impairment loss is recognised in profit or loss as described below.

An asset is impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition, the estimated recoverable value of the asset has been reduced. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

1. **ACCOUNTING POLICIES - continued**

The recoverable amount of goodwill is derived from measurement of the present value of the future cash flows of the business. Any impairment loss is allocated first to the goodwill, and then to other assets on a pro-rata basis. The Company considers there to be no one CGU for the purpose of goodwill impairment.

Where indicators exist for a decrease in impairment loss, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised. Where a reversal of impairment occurs, the reversal is applied to the assets (other than goodwill) on a pro-rata basis. Goodwill impairment is not reversed.

Borrowing costs capitalised

Borrowing costs which are directly attributable to the construction of qualifying tangible fixed assets are capitalised as part of the cost of those assets. Qualifying tangible fixed assets are considered to be those of significant size or complexity, which typically are under construction for in excess of one year and/or where project costs exceed a pre-determined threshold. The commencement of capitalisation begins when both finance costs and expenditures for the asset are being incurred and activities that are necessary to get the asset ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the asset ready for use are complete. Borrowing costs are not capitalised in respect of construction projects which do not meet the defined thresholds or relate to replacement expenditure.

Leases

i. Finance leases

Assets held under finance leases, hire purchase contracts and other similar arrangements, which confer rights and obligations similar to those attached to owned assets, are capitalised as tangible fixed assets at the fair value of the leased asset (or, if lower, the present value of the minimum lease payments as determined at the inception of the lease) and are depreciated over the shorter of the lease terms and their useful lives. The capital elements of future lease obligations are recorded as liabilities, while the interest elements are charged to the profit and loss account over the period of the leases to produce a constant periodic rate of interest on the remaining balance of the liability.

ii. Operating leases

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis. Benefits received and receivable as an incentive to sign an operating lease are similarly spread on a straight-line basis over the lease term.

Provisions

A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are discounted where the impact of discounting the expected future cash flows is material.

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Company's accounting policies, which are described in note 1, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

Critical accounting judgements

a. Cost classification - the allocation of overhead costs to capital investment projects is subject to accounting judgement, particularly around the amount of time spent on different activities. Guidelines have been established, and a Cost Allocation Model is used as part of a process to determine the split of attributable overheads between capital expenditure and operating expenditure.
b. Componentisation of replacement expenditure - As set out in note 1, capitalised replacement expenditure is allocated to mains and services components with a range of useful economic lives between 55 and 65 years. On transition to FRS 102, all replacement expenditure incurred since 2005 has been assessed and allocated on an appropriate and relevant basis where replacement projects have involved multiple activities, judgement has been exercised to determine the appropriate accounts.

Key source of estimation uncertainty

a. Useful lives of assets and residual value - in assessing the estimate of useful economic lives and residual value, consideration is given to the economic life of the gas industry. The depreciation policy is set out in note 1.
b. Retirement benefit schemes - the assumptions used in accounting for the defined benefit pension scheme are based on estimates and are subject to uncertainties. These assumptions are set out in the employee benefit obligations note and include: the discount rate on scheme liabilities, mortality rates, pension increases, salary increases and inflation. The Company takes advice from independent actuaries on the appropriateness of these assumptions
c. Valuation of financial instruments - where financial instruments are recognised at fair value there are uncertainties in forward yield curves used in discounted cash flow calculations.
d. Environmental provision - in assessing the degree of contamination at the various sites estimation is required where elements of the contamination are underground. In these cases, it is difficult to assess with any certainty the extent of the contamination. The discount rate is also a source of estimation.
e. Revenue recognition - Turnover includes an assessment of transportation services supplied to customers between the date of the last meter reading and the year end. Where revenues received or receivable differ from the amount permitted by regulatory agreements, adjustments will be made to future prices to reflect this over or under recovery.

3. EMPLOYEES AND DIRECTORS

The Company had 556 full time equivalent employees as at 31 March 2019 (2018: 606). The average monthly number of full time equivalent employees during the year was 576 (2018: 632).

The Directors received remuneration totalling £43,395 (2018: £45,000) for their services to the Company during the year. No retirement benefits are accruing in the year or in the prior year to any Directors under money purchase or defined benefit schemes, in respect of their services to the Company. The company does not consider there to be any other remunerated key management personnel.

Staff costs for the Company during the year are as follows:

	2019 £m	2018 £m
Wages and salaries	26	28
Social security costs	3	3
Pension costs	16	18
	45	49

4. INTEREST RECEIVABLE AND SIMILAR INCOME

	2019 £m	2018 £m
Interest receivable on loans to other group undertakings	-	2
Other interest receivable	3	2
Net interest on defined benefit liability	3	-
	6	4

5. INTEREST PAYABLE AND SIMILAR CHARGES

	2019 £m	2018 £m
Movement in financial derivatives	3	2
Other interest payable on bonds	99	91
Index linked bond interest	27	27
Unwind of discount	1	1
Other interest payable	-	1
	130	122

No borrowing costs have been capitalised during the year.

6. PROFIT BEFORE TAXATION

The profit is stated after charging/(crediting):

	2019 £m	2018 £m
Depreciation - owned assets	109	104
(Profit)/loss on disposal of fixed assets	(1)	1
Goodwill amortisation	6	6
Computer software amortisation	9	8
Amortisation of customer contributions	(5)	(5)
Operating lease rentals	3	2
Distribution costs	435	433

Auditor's remuneration comprises £68,000 (2018: £73,000) in respect of statutory audit services, £52,000 (2018: £50,000) in respect of other services pursuant to legislation.

7. TAXATION

Analysis of the tax charge

The tax charge on the profit for the year was as follows:

	2019 £m	2018 £m
Current tax:		
UK corporation tax	53	47
Prior period adjustment	(3)	(2)
Total current tax	50	45
Deferred tax:		
Deferred tax	(7)	(9)
Prior period adjustment	1	2
Total deferred tax	(6)	(7)
Tax on profit	44	38

7. **TAXATION - continued**

Reconciliation of total tax charge included in profit and loss
The tax assessed for the year is lower than the standard rate of corporation tax in the UK. The difference is explained below:

	2019	2018
	£m	£m
Profit before tax	242	198
Profit multiplied by the standard rate of corporation tax in the UK of 19% (2018 - 19%)	46	38
Effects of:		
Adjustments to tax charge in respect of previous periods	(2)	-
Non-deductible goodwill	1	1
Profit on disposal of non qualifying assets assets	(1)	(1)
Total tax charge	44	38

Tax effects relating to effects of other comprehensive income

		2019	
	Gross	Tax	Net
	£m	£m	£m
Gains arising on cash flow hedges	1	-	1
Remeasurement net defined benefit asset	(9)	2	(7)
	(8)	2	(6)

		2018	
	Gross	Tax	Net
	£m	£m	£m
Gains arising on cash flow hedges	1	-	1
Remeasurement net defined benefit asset	106	(18)	88
	107	(18)	89

The standard rate of corporation tax applied to reported profit on ordinary activities is 19% (2018: 19%)

A reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) was substantively enacted on 26 October 2015. Further reductions to 17% (effective 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the company's future current tax charge accordingly. The deferred tax asset at 31 March 2019 has been calculated based on these rates. There is no expiry date on timing differences, unused tax losses or tax credits.

8. DIVIDENDS

Dividends paid for the year ended 31 March 2019 amount to £68m (42.20p per share) (2018: £1,047m of which £117m was a cash dividend).

The remaining £930m of the dividend in 2018 was due to the repayment of amounts owed from the Company's parent, Scotia Gas Networks Ltd, the dividends have been offset against the historic intercompany balance. No further dividends were proposed.

9. INTANGIBLE FIXED ASSETS

	Goodwill £m	Computer software £m	Totals £m
COST			
At 1 April 2018	288	110	398
Additions	-	5	5
Disposals	-	(4)	(4)
At 31 March 2019	288	111	399
AMORTISATION			
At 1 April 2018	74	73	147
Amortisation for year	6	9	15
Eliminated on disposal	-	(4)	(4)
At 31 March 2019	80	78	158
NET BOOK VALUE			
At 31 March 2019	208	33	241
At 31 March 2018	214	37	251

The goodwill, which arose on the acquisitions of the business by the Company is being amortised on a straight-line basis over 50 years. This is the period over which the Directors estimate that the value of the underlying business acquired is expected to exceed the value of the underlying assets.

A review for impairment of goodwill is carried out at the end of each financial year. No impairment loss has been recorded in the current year or prior years.

10. TANGIBLE FIXED ASSETS

	Freehold property £m	Plant and machinery £m	Computer equipment £m	Totals £m
COST				
At 1 April 2018	72	5,040	76	5,188
Additions	6	278	7	291
Disposals	-	(54)	(23)	(77)
At 31 March 2019	78	5,264	60	5,402
DEPRECIATION				
At 1 April 2018	22	884	45	951
Charge for year	4	98	7	109
Eliminated on disposal	-	(47)	(23)	(70)
At 31 March 2019	26	935	29	990
NET BOOK VALUE				
At 31 March 2019	52	4,329	31	4,412
At 31 March 2018	50	4,156	31	4,237

Customer contributions

The Company has received customer contributions relating to plant and machinery. In accordance with the Company's accounting policy the assets are capitalised within fixed assets and the contributions are recognised as deferred income in the balance sheet. The connections contributions are from customers being connected to the network and replacement contributions are related to the diversion of gas mains. The deferred income is released to the profit and loss account over the estimated lives of the related assets. The amount deferred under this policy was as follows:

	Connections 2019 £m	Replacement 2019 £m	Total 2019 £m
Customer contributions brought forward	141	58	199
Customer contributions received in year	13	22	(35)
Amortisation in year	(4)	(1)	(5)
	150	79	229

11. DEBTORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2019 £m	2018 £m
Trade debtors	71	63
Derivative financial instruments	-	2
Prepayments and accrued income	8	9
	79	74

12. SHORT TERM DEPOSITS

	2019 £m	2018 £m
Short term deposits	-	266

13. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2019 £m	2018 £m
Bank loans and overdrafts (see note 15)	10	400
Trade creditors	26	11
Amounts owed to group undertakings	28	21
Social security and other taxes	40	39
Other creditors	7	12
Other accrued interest	37	36
Deferred income	21	21
Other accruals	74	85
	243	625

Included in bank loans and overdrafts falling due within one year, are loans and bonds consisting of:

	2019 £m	2018 £
£300m 5.125% fixed rate due 2018	-	300
£50m floating rate EIB maturing 2018	-	50
£50m floating rate EIB maturing 2019	-	50
£10m revolving credit facility	10	-
	10	400

14. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	2019 £m	2018 £m
Bank loans (see note 15)	2,799	2,632
Derivative financial liabilities - mirror swaps	35	43
	2,834	2,675

14. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR - continued

Included in bank loans falling due after more than one year, are bonds consisting of:

	2019 £m	2018 £m
Fixed rate and index linked:		
£250m 2.013% index linked due 2035	249	240
£150m 2.066% index linked due 2025	224	217
£15m 2.580% index linked due 2028	20	19
£215m 4.875% fixed rate due 2020	215	215
£375m 4.875% fixed rate due 2029	374	374
£225m 6.38% fixed rate due 2040	224	224
£300m 4.875% fixed rate due 2023	299	299
£350m 2.5% fixed rate due 2025	347	347
£400m 3.1% fixed rate loan notes due 2036	397	397
£75m fixed rate due 2030	75	-
£75m fixed rate due 2033	75	-
	2,499	2,332
Floating rate:		
£125m floating rate note due 2025	125	125
£80m floating rate note due 2026	80	80
£60m floating rate loan note due 2026	60	60
£35m floating rate loan note due 2026	35	35
	300	300
Total bonds	2,799	2,632

The above borrowings are unsecured and are stated after the deduction of unamortised issue costs of £9m (2018: £10m). These costs together with the interest expense are allocated to the profit and loss account over the term of the borrowings. Interest is calculated using the effective interest rate method.

Certain interest costs in respect of index-linked bonds are not payable until the principal amount of the bond is repaid and are included within the carrying value of the borrowings stated above. The amount included in the carrying value of the borrowings at 31 March 2019 is £162m (2018: £145m).

The total revolving credit facility is £240m and expires in March 2023. £10m of the facility has been drawn at the year end.

Included within creditors falling due after more than one year are derivatives at fair value through profit and loss with a net fair value of £35m (2018: £43m), which are subject to net settlement provisions with a single counterparty. This portfolio comprises long dated pay fixed/receive floating interest rate swaps originally taken out in 2005-06 to fix the Company's interest cost over periods out to 2025, together with pay floating/receive fixed swaps taken out at a later date. The cash flow payment dates and floating leg payment terms match off, although the fixed interest payable on the offsetting swaps is in excess of the original swaps. Changes in the fair value of the portfolio on a net basis are recognised in the profit and loss account as they arise.

15. LOANS

An analysis of the maturity of bonds and bank loans is given below:

	2019	2018
	£m	£m
Between one and five years	513	513
After five years	2,286	2,119
	2,799	2,632
On demand or within one year	10	400
	2,809	3,032

16. FINANCIAL INSTRUMENTS

The Company's funding, liquidity and exposure to interest rate, foreign currency exchange and credit risks are managed within a framework of policies and guidelines authorised by the Board of Directors. In accordance with these policies, and in accordance with covenants set out as part of bond issuances made by the Company, financial derivatives are used to manage financial exposures.

The Company is a wholly owned subsidiary of SGN MidCo Limited and accordingly is, under FRS 102 exempt from the disclosures required under sections 11 and 12 as these are detailed in the annual report of Scotia Gas Networks Limited.

17. PROVISIONS FOR LIABILITIES

	2019	2018
	£m	£m
Deferred tax	523	531
Other provisions		
Other provisions	5	6
Environmental provisions	8	23
	13	29
Aggregate amounts	536	560

17. **PROVISIONS FOR LIABILITIES - continued**

	Deferred tax £m	Other provisions £m
Balance at 1 April 2018	531	29
Unwinding of discounted amount	-	1
Utilised during year	-	(1)
Net movement in deferred tax	(8)	-
Arising during the year	-	(1)
Disposals	-	(15)
Balance at 31 March 2019	523	13

Environmental
The environmental provision represents the Directors' best estimate of environmental restoration costs, where the Company has a legal obligation to restore sites at the balance sheet date. The provision has been discounted and is stated at the present value of the expenditure expected to be required to settle the obligation. The provision is expected to be utilised over the next thirteen years.

Other provisions
Other provisions include asbestos related liabilities. The provision has been discounted and is stated at the present value of the estimated expenditure to settle the obligation. The provision is expected to be utilised over the next 31 years.

Deferred tax
Deferred tax is provided as follows:

	2019 £m	2018 £m
Accelerated capital allowances	503	510
Fair value movements in financial derivatives	-	1
Deferred tax on retirement benefit obligations	20	20
Provision for deferred tax	523	531

17. PROVISIONS FOR LIABILITIES - continued

The movement in provision for deferred tax is as follows:

	2019 £m	2018 £m
Opening balance	531	520
Credited to profit and loss account	(6)	(7)
Movement through reserves	(2)	18
Provision for deferred tax	523	531

Deferred tax has been measured based upon corporation tax rates substantively enacted at the balance sheet date. (Information regarding rates of corporation tax can be found in taxation note in notes to the financial statements.)

Deferred tax assets and liabilities are offset only where the Company has a legally enforceable right to do so and where the assets and liabilities relate to income taxes levied by the same taxation authority on the same taxable entity or another entity within the Company.

The Company has no unrecognised deferred tax assets or liabilities.

18. ACCRUALS AND DEFERRED INCOME

	2019 £m	2018 £m
Accruals and deferred income	229	199

19. CALLED UP SHARE CAPITAL

Allotted, issued and fully paid:

Number:	Class:	Nominal value:	2019 £	2018 £
160,174,772	Ordinary	£1	160,174,772	160,174,772

20. RESERVES

	Profit and loss account £m	Hedge reserves £m	Totals £m
At 1 April 2018	737	(1)	736
Profit for the year	198	-	198
Dividends	(68)	-	(68)
Movement in cash flow hedges	-	1	1
Defined benefit pension asset	(7)	-	(7)
At 31 March 2019	860	-	860

The hedging reserve represents the cumulative portion of gains and losses on hedging instruments deemed effective in hedging variable interest rate risk of recognised financial instruments or foreign exchange risk in firm commitments or highly probable forecast transactions. Amounts accumulated in this reserve are reclassified to profit or loss in the periods in which the hedged item affects profit or loss or when the hedging relationship ends.

A proportion of dividends paid in 2018 is due to the repayment of amounts owed from the Company's parent, Scotia Gas Networks Limited, the dividends have been offset against the historic intercompany balance.

21. EMPLOYEE BENEFIT OBLIGATIONS

Defined contribution schemes

The Company operates a defined contribution retirement benefit schemes for all qualifying employees of the Group.

The amount recognised in the profit and loss account is as follows:

	2019 £m	2018 £m
Amount charged in respect of defined contribution schemes	5	3

21. EMPLOYEE BENEFIT OBLIGATIONS - continued

Defined benefit schemes

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks which operates the Scotia Gas Networks Pension Scheme, a defined benefit scheme for a significant number of its employees of its subsidiaries who prior to 1 December 2005 were previously members of the Lattice Company Scheme and had joined prior to 31 March 2002. Employees joining the Lattice Company Scheme after 31 March 2002 were entitled to join a defined contribution scheme. Under the Group cost allocation plan, the Company accounts for its agreed share of the total net defined benefit cost, based on the proportionate members relating to the Company.

The most recent full actuarial valuations of scheme assets and the present value of the defined benefit obligation were carried out at 31 March 2015, a limited actuarial review has been carried out by Hymans Robertson LLP at 31 March 2019. The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method.

	As at 31 March 2019	As at 31 March 2018
Key assumptions used:		
Retail price inflation	3.4% p.a.	3.2% p.a.
Consumer price inflation	2.4% p.a.	2.2% p.a.
Pension increase rate RPI	3.4% p.a.	3.2% p.a.
Salary increase rate	3.2% p.a.	3.0% p.a.
Discount rate	2.3% p.a.	2.7% p.a.

The discount rate is based on the return of high quality corporate bonds.

The assumptions relating to longevity underlying the pension liabilities reflect the characteristics of the Scheme membership ('VitaCurves') for base mortality, with an allowance for further improvements in life expectancy in line with the medium cohort adjustments subject to a 1.5% p.a. underpin in the longevity assumption. The assumed life expectations on retirement at age 65 are:

As at 31 March	2019		2018		2017	
	Male	Female	Male	Female	Male	Female
Members currently aged 65	22	24	22	24	24	25
Members currently aged 45	24	27	24	26	27	28

21. EMPLOYEE BENEFIT OBLIGATIONS - continued

The approximate effects of movements in the main assumptions on the defined benefit obligation are shown in the table below:

	Sensitivity	Approximate change in DBO £000
Discount rate	+ 0.1% p.a.	10,598
	- 0.1% p.a.	11,060
Price inflation (RPI measure)*	+ 0.1% p.a.	9,534
	- 0.1% p.a.	9,064
Life expectancy	+ 1 year	21,488
	- 1 year	(20,656)

*These movements have been calculated assuming that changes in the inflation assumption have a knock-on effect on the pension increase and salary growth assumptions (i.e. the "real" increase rates are maintained). Note that the sensitivities do not allow for the movement in the insured pensioner asset, therefore the net balance sheet movement is smaller.

The analysis of scheme assets and the amount included in the balance sheet arising from the Company's obligations in respect of its defined benefit retirement benefit schemes at the balance sheet date is as follows:

As at 31 March	2019			2018		
	Quoted	Unquoted	Tot:	Quoted	Unquoted	Tot:
	Fair Value £m	Fair Value £m	Fair Value £m	Fair Value £m	Fair Value £m	Fair Value £m
Equities	123	-	123	157	-	157
Government bonds [2]	285	-	285	212	-	212
Corporate bonds	203	-	203	169	-	169
Property	1	-	1	13	-	13
Cash	4	-	4	21	-	21
Insurance contracts	-	52	52	-	49	49
Total market value of assets	616	52	668	572	49	621
Actuarial value of liabilities			(548)			(504)
Net pension asset			120			117

[2] Including LDI repurchase agreement liabilities.

21. EMPLOYEE BENEFIT OBLIGATIONS - continued

The fair value of scheme assets at 31 March 2019 are based on the bid price where available. The fair value of property is based on the mid price and the value of the single unit price funds is based on the single unit price.

To reduce the risk of volatility in the Scheme's funding level, a liability driven investment (LDI) strategy forms part of the assets employed within the investment strategy of the Scheme. The LDI strategy provides c71% interest rate protection and c81.5% inflation protection as at 31 March 2019 with respect to the pension scheme liabilities of c.£1.34bn (valued using a UK government bond yield curve). The Scheme assets which provide this interest rate and inflation protection are managed by BlackRock and Goldman Sachs and include a variety of instruments e.g. UK government bonds (gilts), interest rate swaps, inflation swaps, gilt repos and corporate bonds. The Scheme has implemented a pensioner buy in which also contributes to the total interest rate and protection ratios referred to above.

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

	2019 £m	2018 £m
Opening defined benefit obligation	(504)	(690)
Current service cost	(10)	(14)
Administration costs	(1)	-
Interest cost	(13)	(16)
Actuarial (losses)/gains	(56)	94
Benefits paid	36	122
Closed defined benefit obligation	(548)	(504)

Movement in the fair value of scheme assets were as follows:

	2019 £m	2018 £m
Opening fair value of scheme assets	621	693
Interest income on scheme assets	16	17
Contributions from Southern Gas Networks Plc	21	21
Remeasurement of scheme assets	47	12
Benefits paid	(36)	(122)
Administration costs	(1)	-
Closing fair value of scheme assets	668	621

The actual gain on scheme assets was £64m (2018: £25m).

21. EMPLOYEE BENEFIT OBLIGATIONS - continued

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

	2019 £m	2018 £m
Current service cost	(10)	(14)
Administration costs	(1)	-
Total charged to operating profit:	(11)	(14)
Expected return on scheme assets	16	16
Interest charge on scheme liabilities	(13)	(16)
Net interest credit/(cost)	3	-
Total charge to the profit and loss account	(8)	(14)

	2019 £m	2018 £m
Actuarial gains/(losses) on scheme assets	47	12
Actuarial (losses)/gains on scheme obligations	(56)	94
(Losses)/gains recognised in other comprehensive income	(9)	106

22. FINANCIAL COMMITMENTS

Capital projects contracted for by the Company but not provided in the financial information amounted to £33m at 31 March 2019 (2018: £17m). Within this amount £10m (2018: £4m) is related to intangible assets.

Total future minimum lease payments under non-cancellable operating leases for the Company are as follows:

	Other		Land and Buildings	
	2019 £m	2018 £m	2019 £m	2018 £m
- less than one year	1	2	1	-
- between two to five years	2	3	1	1
- after five years	-	-	12	11

23. RELATED PARTY DISCLOSURES

The immediate parent undertaking is SGN MidCo Limited.

The ultimate parent undertaking is Scotia Gas Networks Limited, a Company registered in England and Wales.

Scotia Gas Networks Limited is owned by a consortium consisting of SSE plc (33%), Borealis Infrastructure Europe (UK) Limited (25%) which is indirectly wholly owned by OMERS Administration Corporation, OTPPB Investments (UK) Limited (25%), which is owned by Ontario Teachers' Pension Plan Board, and Blue Spyder B 2016 Limited (17%), which is owned by Abu Dhabi Investment Authority. It is the opinion of the Directors that the parent Company, Scotia Gas Networks Limited, has no single controlling party as that Company is controlled jointly by the consortium.

In accordance with FRS102 the Company is exempt from disclosing transactions with subsidiaries that are wholly-owned by the group.

Transactions with shareholders
Amounts owed to shareholders and loans from shareholders are set out below:

	2019 £m	2018 £m
Other amounts owed to shareholders:		
SSE plc	8	9

The amounts owed to shareholders mainly comprise amounts payable in respect of a managed service agreement for corporate services and material purchases.
The following transactions took place during the year between the Company and the SSE plc group of companies ("SSE").

	2019 £m	2018 £m
Sales of goods and services	92	94
Purchase of goods and services	(29)	(28)

Sales of goods and services to SSE primarily represent gas transportation services. At 31 March 2019 an amount of £nil was owed by SSE in relation to these services.

SSE provides services to the Company in the form of a management services agreement for corporate services. The Company also purchases certain items such as consumables stock, shrinkage gas and public liability insurance from SSE.

24. SUBSEQUENT EVENTS

There are no subsequent events to report.