Registered Number: 9223384

# WESTERN POWER DISTRIBUTION PLC AND SUBSIDIARY UNDERTAKINGS

ANNUAL REPORT AND FINANCIAL STATEMENTS

For the year ended 31 March 2020



Serving the Midlands, South West and Wales

## **Western Power Distribution plc**

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#### Strategic report

For the year ended 31 March 2020

The directors present their annual report and the audited financial statements of Western Power Distribution plc and its subsidiary undertakings (the "WPD Group" or "WPD") for the year ended 31 March 2020. These are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union ("EU").

#### Group background

WPD Group mainly comprises the four Distribution Network Operators ("DNOs"): Western Power Distribution (South West) plc ("WPD South West"), Western Power Distribution (East Midlands) plc ("WPD East Midlands"), and Western Power Distribution (West Midlands) plc ("WPD West Midlands").

In addition to the DNOs, the Group also consists of other smaller subsidiaries including WPD Smart Metering Limited, WPD Telecoms Limited and South Western Helicopters Limited. The primary purpose of these businesses is to support the DNO and network related activities of the Group. The Group also owns property companies, to facilitate the management of non-network and investment properties of the Group.

#### Ownership

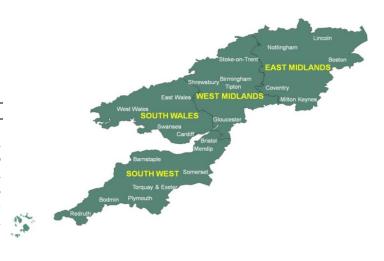
The WPD Group is owned by Western Power Distribution Plc, which is a public limited company owned by one shareholder, PPL Corporation. PPL Corporation is an electricity utility based in Allentown, Pennsylvania, United States of America.

#### **Business model**

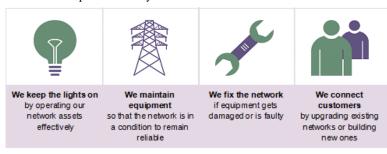
WPD is the electricity Distribution Network Operator for the Midlands, the South West and South Wales. Our combined network is the largest in the UK, with our four DNOs delivering electricity to approximately 7.9 million (2019: 7.9 million) customers and employing around 6,600 (2019: 6,600) staff.

	Customers (million)	Area (sq km)
WPD South West	1.6	14,400
WPD South Wales	1.1	11,800
WPD East Midlands	2.7	16,000
WPD West Midlands	2.5	13,300
	7.9	55,500

The 7.9 million customers are registered with licensed electricity suppliers, who in turn pay the WPD Group for use of the network. Our costs are regulated and based on the Office of Gas and Electricity Markets Authority's ("Ofgem's") estimates; the average GB customer in 2019/20 will pay £90 per year in real 2018/19 price terms for electricity distribution costs.



What we do comprises four key tasks:



The Group's network comprises approximately 90,000km (2019: 90,000km) of overhead lines, 136,000km (2019: 135,000km) of underground cable and 189,000km (2019: 188,000km) transformers.

#### Regulation

The DNOs are monopolies regulated by the Gas and Electricity Markets Authority, which operates through Ofgem.

The regulatory framework is based on sustainable network regulation, known as the "RIIO" model where Revenues=Incentives+Innovation+Outputs. From 1 April 2015 Ofgem set an eight year electricity price control (known as RIIO-ED1). Under the RIIO model there is an emphasis on companies playing a full role in developing a more sustainable energy sector and delivering value for money network services for customers. A key feature of the RIIO model is that the setting of outputs that network companies are expected to deliver is much more extensive with the outputs embedded within an overall Business Plan that was influenced through engagement with our stakeholders. Progress against our business plan is published annually on our website at the link below:

https://www.westernpower.co.uk/customers-and-community/performance-reporting-riio-ed1

For the year ended 31 March 2020

#### **Regulation (continued)**

The operations are regulated under the distribution licence which sets the requirements that WPD needs to deliver for its customers and the associated revenues it is allowed to earn for the eight-year period from 1 April 2015 to 31 March 2023.

In addition to the base level of revenue which the DNOs are allowed to earn, there are incentives to innovate, and incentives relating to customer satisfaction, complaints handling, stakeholder engagement, connections and supply interruptions. The achievement or not of these targets can result in revenue penalties or rewards relating to these activities.

WPD submitted an outputs based Business Plan for the RIIO-ED1 period (2015-2023), which was accepted by Ofgem as "well justified" and could therefore "fast-track" all four WPD licensed areas, ahead of the other five licensed distributor groups. WPD's modified licences took effect from 1 April 2015.

Our RIIO-ED1 business plan is available at the link below:

https://www.westernpower.co.uk/customers-and-community/our-riioed1-business-plan

#### Long term strategy

Our strategy is to deliver outstanding operational performance for all of our customers, support a sustainable energy future, meet our stakeholder requirements and maintain financial stability.

Ensuring that WPD is prepared for the future is a key factor in delivering our strategy and our key actions in this regard are:

#### - Understanding the load related needs of the network

Network monitoring, independent information sources and modelling techniques are used by WPD to predict investment requirements into the long term. WPD also monitors fault rates and undertakes analysis of causes which enables targeted investment programmes to be established. This is then embedded into the continuous asset replacement forecasts.

#### - Adapting to change

Adapting to change is an integral part of what we do; we are used to adopting technological innovation to create a more cost effective electricity network. The transition to a Distribution System Operator ("DSO") will help WPD to be ready for future challenges. Through implementation of our DSO Transition Programme, we are building on our Future Networks Programme to ensure that our network, and our business, has the capacity to deliver all the emerging system requirements our customers have, both now and in the future.

On flexibility our Flexible Power product has transitioned to business as usual with two tender rounds per annum. Our last round contracted with 123 megawatts of flexibility. Our next (fourth) round is seeking 334 megawatts of flexibility required to operate over the summer and winter of 2020 and could potentially defer over £40m of conventional reinforcement. It also delivered on the 'Flexibility First' commitment made by all DNO CEOs to fully test the market ahead of undertaking conventional reinforcement.

WPD leads on the Electricity Networks Association's ("ENA's") open networks project, which is helping to coordinate DSO transition at an industry level. Following consultation with stakeholders, the project is focusing on:

- Processes to develop flexibility services;
- Whole electricity system planning;
- Visibility of information to stakeholders;
- Implementation of short term customer service improvement such as queries management.

#### - Investing in technology and innovation

Innovation is core to our business strategy. Developing better ways of doing things is encouraged throughout the business. Innovative ideas are captured, tested and rolled-out into the business on a regular basis. We look for innovative developments across the following broad areas:

- Network performance and efficiency developing better processes, searching out equipment and technology developments that ensure we continue to be efficient and effective;
- Customer service developing smarter ways of delivering outstanding levels of customer service;
- Environment reducing our business impact on the environment;
- Low carbon networks supporting future electricity demand and generation requirements.

#### Key goals

Our five key goals that underpin our long term strategy are: Safety, Network Performance & Security, Financial Stability, Environment and Stakeholder Value & Engagement.

For the year ended 31 March 2020

#### **Key goals (continued)**

These five key goals align to our RIIO-ED1 business plan including our 76 commitments, details of which can be found here: <a href="https://yourpowerfuture.westernpower.co.uk/performance-reporting-riio-ed1">https://yourpowerfuture.westernpower.co.uk/performance-reporting-riio-ed1</a>

#### Safety

Safety is the highest priority at WPD. WPD continuously promotes safety, both within the business and externally to groups such as school children, land owners and construction operators through activities such as safety awareness and education sessions as well as distributing safety related information.

To support this goal, robust safety policies are in place that are designed based on the assessment of the hazards and risks involved with a particular activity and are further enhanced in response to incidents that have occurred in WPD and other businesses and to changes in legislation.

WPD's safety management system is compliant with the requirements of British Standard, OHSAS 18001 (Occupational Health and Safety Assessment Series) and this involves staff continuously looking for opportunities to enhance safety. WPD staff play an active role in many national committees and steering groups which concentrate on the future of safety and training policies and practices across the industry.

Continuous learning from incidents or near misses is a key objective. Incidents are proactively investigated and suitable changes are put in place to reduce the likelihood of a recurrence.

Our detailed safety policy can be found at:

 $\underline{https://www.westernpower.co.uk/customers-and-community/health-safety}$ 

#### Network performance & security

WPD is committed to providing a secure, reliable and continuous network connection to its customers. We look at the physical security aspects of our network and at preventing any cyber breach incidents. WPD recognises that our information systems and electricity networks are critical and valuable assets that must be protected and thus is focused on maintaining a robust system of cyber security that enables business continuity, minimises operational risk and preserves individual data privacy.

#### Financial stability

Delivering solid financial results to ensure long term viability and stability is another of the key goals of WPD. Our revenue is largely fixed across a price review period and is set at a level that should meet our efficient operating costs and expenses over that period, as well as funding efficient investment, interest on necessary borrowings and the payment of all applicable taxes. In order to encourage investment, our allowed revenue also allows for a return to shareholders.

#### **Environment**

WPD is dedicated to conducting its business as a responsible steward of the environment. WPD monitors its impact in terms of carbon footprint, waste recycling and fluid loss.

Every member of staff is made aware of WPD's environmental commitment to abide by environmental laws, regulations and corporate environmental policies, and their responsibilities for reporting any concerns on potential environmental compliance issues so that appropriate action can be taken.

As a result of our environmental policies, we have been able to maintain our accreditation to the ISO14001:2015 environmental management standard.

More detailed information on our environmental goals can be found in our published report available at: <a href="https://www.westernpower.co.uk/customers-and-community/environment">https://www.westernpower.co.uk/customers-and-community/environment</a>

#### Stakeholder value & engagement

The success of our business is critically dependent on the way we work with our key stakeholders. We aim to create value for our existing stakeholders every day and take account of our future stakeholders and their evolving needs. We regularly engage with key stakeholders to ensure that our goals and objectives are in line with their expectations. Our key stakeholders being:

#### - Customers

WPD strongly believes that customer satisfaction and feedback is the key to the future success of the business.

WPD continues to strive for greater efficiency with regard to operating costs, seeking innovative ways to reduce both the time and cost to repair and replace assets. This approach aims to minimise the cost to the customer of running and maintaining the network.

For the year ended 31 March 2020

#### **Key goals (continued)**

#### Stakeholder value & engagement (continued)

#### - Customers (continued)

WPD's commitment to customer satisfaction is demonstrated by its continued accreditation to the Customer Service Excellence ("CSE") Standard. WPD has held the charter mark of best practice since 1992 - the only energy company in the UK to do so. The CSE assessor visits contact centres and local depots every year and stringently assesses WPD's engagement activities, including delivery, timeliness, information, professionalism and staff attitudes. 57 elements are assessed and WPD now has 45/57 (2019: 44/57) at 'compliance plus' level, demonstrating UK-wide best practice.

Customer awareness is a key commitment for WPD and we engage in ongoing communications so that the Group's customers are more informed regarding matters impacting them. WPD conducts an annual customer awareness campaign "Power for life" that makes contact with every customer using direct mail to homes and businesses, as well as a four-week television and radio campaign, press releases and social media. While reinforcing who we are, what we do, and how well we do it, the campaign also provides information and advice, and explains how we can be contacted in an emergency.

#### - Employees

Our business is built by our people and WPD is fully committed to keeping its employees motivated and actively involved.

Equality of opportunity is key to WPD's approach to hiring, training and promoting employees. WPD holds the British Service Standard for diversity and inclusion and acknowledges the value that a diverse workforce brings to the organisation. We have an established Equality and Diversity policy demonstrating the equal treatment of all existing and future employees.

Employees are selected, treated, and promoted according to their abilities and merits and to the requirements of the job. Applications for employment by people with disabilities are fully considered, and in the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Company continues by way of making adjustments to their role and/or working environment or through retraining arranged as appropriate. 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.

In addition WPD provides an ethics helpline that employees can use to report any concerns.

#### - Suppliers

We rely on quality, value for money goods and services from reputable suppliers and contractors in order to maintain the highest standards in network reliability and customer service. WPD maintains open and positive communication with all suppliers and contractors and treats them fairly, evenly and with honesty.

#### - Regulators

WPD has a helpful and transparent approach in its dealings with the industry regulator, Ofgem, on all matters guiding and impacting energy distribution in the UK.

WPD has a significant role to play in supporting the Government's move to deliver a low carbon economy. WPD is engaging with Ofgem, to help develop a regulatory price control framework which contains the right customer focused outputs and economic incentives to help deliver the Government's objective.

WPD continues to promote transparency of performance and returns. WPD's Regulatory Financial Performance Reporting provides clear and transparent information on WPD's financial and operational performance from a regulatory perspective, including WPD's performance against incentives under the RIIO price control arrangements, and the Return on Regulatory Equity earned for the period.

WPD also strategically and operationally engages with the Health and Safety Executive ("HSE"). Steps in this regard are:

- WPD's CEO and senior managers attend national groups such as the National Health & Safety Committee ("HESAC"), of which the HSE is a member;
- WPD's CEO and senior managers meet with key HSE staff throughout the year to discuss matters and where appropriate collaborate on strategic Health and Safety issues and initiatives;
- WPD aligns its internal safety campaigns to the HSE 'Helping Great Britain Work Well' safety message and separately the HSE supported, National HESAC led 'Powering Improvement' H&S programme.

Another key regulator for WPD is the Environment Agency ("EA"), which monitors areas such as pollution prevention, habitat conservation and other matters relating to the protection and enhancement of the environment in England. WPD continuously works together with the EA to improve its environmental performance. Similarly WPD also engages with National Resources Wales ("NRW"), as the environmental regulator for South Wales.

For the year ended 31 March 2020

#### **Key goals (continued)**

#### Stakeholder value & engagement (continued)

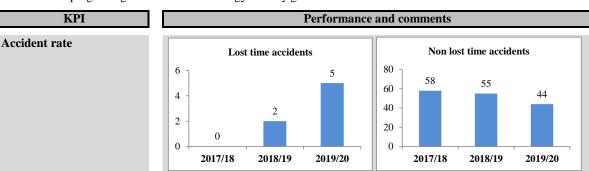
#### - Shareholder

Safety

The WPD Group is ultimately owned by PPL Corporation. WPD is committed to providing its shareholder with long term, sustainable value.

#### **Key performance indicators (KPIs)**

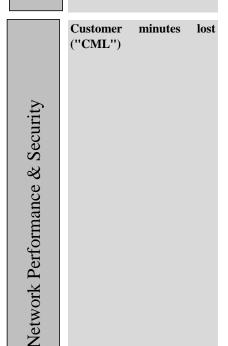
WPD utilises KPIs to assess progress against the overall strategy and key goals.

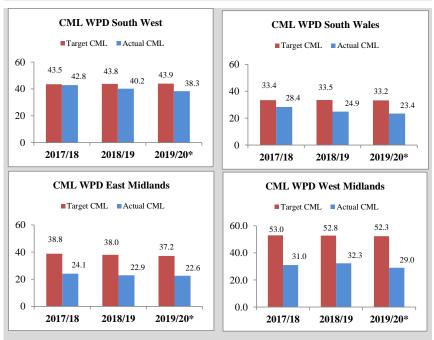


Electricity distribution carries inherent safety risks and the WPD directors are committed to the highest levels of safety in all areas. All accidents are investigated and we ensure that all our planned inspection and maintenance programmes are completed during the year. While lost time accidents rose slightly during the year, the WPD Group's rolling lost time accident frequency rate per 100 people as at 31 March 2020 is at 0.076 against a regulatory target of 0.145 (48% below the output measure). The total number of accidents to staff across the WPD Group decreased from 57 in 2018/19 to 49 in 2019/20.

In addition WPD monitors the overall rate of accident per 100 employees (as reported to Ofgem). The accident rate for the WPD Group for 2019/20 is 0.75 (2018/19: 0.86), which is below the RIIO-ED1 target of 1.6 (a reduction of 10% over the price control prior to RIIO-ED1). Further details on our performance reporting to Ofgem regarding safety can be found at the link below:

 $\underline{https://www.westernpower.co.uk/customers-and-community/performance-reporting-riio-ed1/safety}$ 





CML represents the average time a customer is without power during the year. It is calculated by taking the sum of customer minutes lost for all incidents, excluding the allowed exceptional events, divided by customers connected. The targets are defined by Ofgem at each DNO level. Year on year WPD is outperforming its targets as we are focused on ensuring complete network reliability for our customers.

\*The 2019/20 actuals are subject to Ofgem

confirmation on excluded events.

#### Key performance indicators (KPIs) (continued) **KPI** Performance and comments Number of customer CI WPD South West CI WPD South Wales interruptions ("CI") ■ Target CI ■ Actual CI ■Target CI ■Actual CI 100 100 80 80 62.0 58.5 51.5 53.3 53.1 60 60 52.7 48.5 46.1 43.4 41.3 40 40 20 20 0 2017/18 2018/19 2019/20\* 2017/18 2018/19 2019/20\* Network Performance & Security CI WPD East Midlands CI WPD West Midlands ■Target CI ■ Actual CI ■Target CI ■Actual CI 100 100 85.4 82.5 80 80 55.6 55.4 51.0 60 50.8 60 48.5 39.8 37.9 40 40 20 20 2017/18 2018/19 2019/20\* 2017/18 2018/19 2019/20\* CI represents supply interruptions experienced by connected customers, per 100 customers. Adjustment for exceptional one off events that are outside the control of DNOs is allowed by Ofgem. The targets are defined by Ofgem at each DNO level. \*The 2019/20 actuals are subject to Ofgem Year on year WPD is performing better than its targets as we are focused on ensuring confirmation on excluded events. complete network reliability for our customers. - In 2019/20 88.0% (2018/19 88.0%) of customers had their power restored within Other measures an hour of a high voltage fault, the target being 87.5%. - One of the guaranteed standards of performance ("GSOPs") set by Ofgem is a reduction in the number of customers left without electricity for more than 12 hours. The number of customers without electricity for more than 12 hours was 270 (2018/19: 26), an improvement of over 97% on our 2012/13 benchmark performance. Customers received a set payment where we failed to achieve the GSOP. 2018/19 The majority of WPD's revenue is fixed across the Revenue 2019/20 (£m) (£m) current price control period. Ofgem sets the revenues at a level that covers reasonable costs and allows a 1,723.5 1,685.6 reasonable rate of return. In addition to the base level of Financial Stability fixed revenue that a DNO can earn, there are incentive measures including customer service outputs, network outputs and innovation, which constitute allowed revenue. **Profit before taxation** 2019/20 2018/19 As part of the regulatory process, Ofgem sets the ("PBT") (£m) (£m) allowed rate of return within each price control, which 749.7 733.2 for RIIO-ED1 is set at 6.4%. As evident from the level of capital expenditure below, WPD invests a significant

proportion of its profits back into the networks to ensure that we continue to provide an efficient, reliable and secure service to our customers. The increase in PBT is due to an increase in revenue during the year.

#### **Key Performance Indicators (KPIs) (continued)**

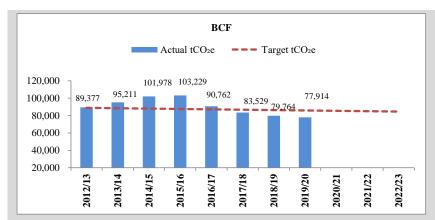
	KPI	Performance and comments				
	Fixed asset additions  Tangible fixed asset additions	2019/20 (£m) 916.3	2018/19 (£m) 882.4	WPD operates in a capital intensive industry and thus invests a major proportion of profits into replacing and adding electricity infrastructure, as evident from the extent of our capital expenditure. Due to the age of the network and technological advancements significant investment is required in capital related activities. During the RIIO-ED1 period to date we have invested £4.8bn in capital related activities. Planned investment in the network for the remainder of the RIIO-ED1 period (until March 2023) is £2.4bn.		
Financial Stability	Regulatory asset value ("RAV")	2019/20 (£m) 7,999.7	2018/19 (£m) 7,698.1	RAV is a regulatory concept to represent assets with a long term life. It is essentially equivalent to the net book value of the fixed assets of the business, only calculated in regulatory terms using methodology provided by Ofgem. It is an important measure for all DNOs as the allowed revenue in any year includes a return on RAV and amortisation of RAV as determined by Ofgem. Other important measures, such as gearing ratios and recoverable amounts of DNOs with respect to impairment calculations, are calculated using RAV. Because of timing the RAV used in these calculations is the latest draft and not the finalised value. Movement in RAV is largely driven by additions to our RAV during the year which are based on 80% of our total expenditure (Totex) calculated in accordance with methodology provided by Ofgem, and after application of the Totex Incentive. It is not possible to perform a reconciliation between RAV and IFRS measures as RAV is a regulatory measure. The differences between IFRS and regulatory rules have built up over many years and cannot be reconciled.		
	Gearing ratio  Net debt* RAV  * Refer to note 24 on page 89 for the calculation of net	2019/20 (£m) 6,199.9 7,999.7	2018/19 (£m) 5,955.2 7,698.1	Gearing for WPD is calculated as the ratio of net debt to RAV. The gearing ratio is monitored in relation to the rolling credit facility covenants for several of the WPD companies and is used as a key internal measure. To comply with bank covenants as well as the internal KPI, the gearing ratio for the WPD Group does not exceed 85%.		
	Interest cover  PBT Finance cost Depreciation Amortisation - intangible assets Amortisation - customer contributions Earnings before interest, taxation, depreciation, and amortisation ("EBITDA") Interest payable Interest cover	2019/20 (£m)  749.7 301.0 240.8  7.4  (46.1)  1,252.8  301.0  4.2	2018/19 (£m)  733.2 282.6 227.7  5.4  (45.3)  1,203.6  282.6  4.3	A minimum ratio of earnings before interest, tax, depreciation and amortisation ("EBITDA") to interest payable is required by credit facility covenants for several of the WPD companies. It is also used as a key internal indicator of the financial health of the DNOs. In order to comply with bank covenants, the interest cover ratio can not fall below 3:1; our interest cover ratio is at an acceptable level and shows a sufficient level of earnings to cover interest payments.		

#### Key performance indicators (KPIs) (continued)



#### Performance and comments

# **Business carbon footprint** ("BCF")



Our BCF details the impact that our operational activities have on the environment in terms of associated carbon dioxide ("CO2") emissions. We report our BCF using equivalent tonnes of carbon dioxide ("tCO2e"). For calculations WPD follows a recognised methodology as described within international business carbon footprint standards, the Greenhouse Gas ("GHG") reporting protocol and ISO14064-1. ISO14064-1 specifies principles and requirements at the organisation level for quantification and reporting of GHG emissions and removals.

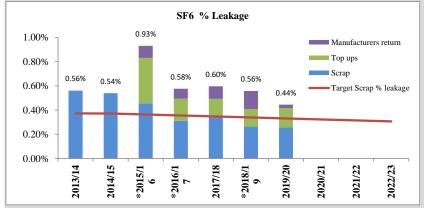
WPD's current target is a 5% reduction over the RIIO-ED1 period based on the baseline year of 2012/13. At 2019/20 we are outperforming our target.

For further details on various elements that make up our BCF refer to our detailed environment report at the link below:

https://www.westernpower.co.uk/customers-and-community/environment

SF6 emissions (emissions as % of SF6 bank) SF6 gas is used throughout our industry as an insulating medium in switchgear. Although it provides many benefits, it is a potent greenhouse gas. There are currently no viable alternatives to SF6. We continue to monitor our SF6 emissions.

The amount of SF6 emitted is expressed as a percentage of the overall 'bank' of switchgear containing SF6, as this will vary over the period of RIIO-ED1. The target is based on an average of emissions between 2009/10 and 2010/11.



Overall the level of leakage is reducing over time as older units are replaced with new units which also contain lower levels of SF6. The WPD's Group's current target is a 17% reduction over the RIIO-ED1 period. The target was set at start of RIIO-ED1 and relates only to scrap % leakage, as the top ups and manufacturers return data was not compiled at that time. When replacing switchgear, we give priority to the switchgear with the highest leak rates. Within RIIO-ED1, we have committed to replacing any 11kV distribution assets that show signs of leakage and any higher voltage assets that have leaked three times. When a leak becomes apparent, we locate its source so that a strategy can be developed to manage the situation, taking into account the potential for repairs and the lead times for replacement switchgear.

\* The prior year data has been updated to provide a more accurate position and include the top ups and manufacturers return leakages.

#### Key performance indicators (KPIs) (continued)

KPI

#### Fluid cable losses

The design of very high voltage underground cables has evolved over many years and our new cables all use a solid plastic like insulation. Old designs of 33kV and higher voltage cables used an insulating oil in ducts inside the cable. Whilst these cables are normally very reliable, in the event of a fault, or damage by third parties, this oil may leak out. In common with other DNOs, WPD works to an operating code agreed with

**Performance and comments** 

the Environment Agency, and assesses both the condition and the environmental risk posed by the fluid filled cables which the WPD Group owns.

Losses in litres Actual Losses --- Target losses 50,000 43,123 43,317 40,000 30,950 30,000 22,216 17,291 17,251 20,000 10,000 2013/14 2014/15 2015/16 2016/17 2017/18 2018/19 2021/22 2022/23 2012/13 2020/21

WPD's current target is a 75% reduction over the RIIO-ED1 period based on the baseline year of 2012/13.

The losses from WPD's fluid filled cables can vary from year to year dependent on the number of small leaks at disparate locations rather than high volume single events, often caused by third parties. Since 2018/19 WPD has improved its technique for the detection of cable fluid losses as well as introduced a better system for loss reporting; this has resulted in a significant reduction in the volume of losses associated with our fluid filled cables for the current reporting year.

\* The prior year data has been updated to provide a more accurate position.

#### Other measures

#### - Environmental management standard

In May 2017, all four DNOs gained certification to the new ISO14001:2015 environmental management standard. ISO14001 sets out the criteria for an environment management system and maps out a framework that an organisation can follow to set up an effective environment management system. A re-certification audit has been completed successfully in May 2020 with no major non-conformances raised and the Group's certification has been extended until June 2023.

#### Customers

# Overall customer satisfaction



As part of Ofgem's Broad Measure of Customer Satisfaction Incentive, a research agency undertakes a monthly satisfaction survey assessing customers' satisfaction for connection quotations and delivery, interruptions and general enquiries. The customer satisfaction score is given out of 10. For WPD's four licence areas around 22,000 customers are surveyed per year. For the regulatory year 2019/20, all WPD licensees received a score greater than 9 out of 10 overall for customer satisfaction.

Ofgem also compared the speed of response that a DNO call centre provides and WPD is consistently identified as the top performer with an average speed of response below 1.63 seconds.

Stakeholder Value & Engagement

Environment

#### KPI

#### **Performance and comments**

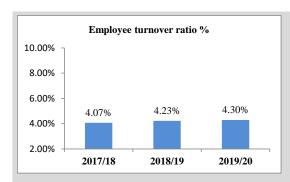
#### Customers (continued)

#### **Stakeholder Engagement Incentive**

WPD has maintained its position as the top performing DNO group in the Stakeholder Engagement Incentive Award Scheme (a key element of Ofgem's Broad Measure of Customer Satisfaction), held since its introduction in 2011/12. Most recently in 2018/19 WPD was again rated first place in the industry (outperforming every DNO, gas and transmission network) with a score of 8.35 out of 10. This was worth £6.35m (2018/19 prices) and will be applied to 2019/20 revenues across the four DNOs. WPD entered three written submissions and attended a question and answer session with an Ofgem-appointed judging panel of experts.

#### **Employees**

#### **Employee turnover ratio**



The turnover ratio includes retirements which is driving the year on year increase. On an overall basis, WPD has a very low employee turnover ratio, indicating high levels of satisfaction and motivation of staff.

#### Gender pay gap





WPD's median gender pay gap for the year ended 31 March 2019 is 10.5%. This is 6.8% below the national gender gap and 13.3% below its industry gender pay gap. Therefore, in relative terms, WPD's gender pay gap is positioned positively compared to its UK-wide industry segment. These comparisons are based on the latest available data. Our median bonus pay gap has continued to remain stable at 0%, while our mean bonus pay gap fell substantially from 59.6% to 13.8% year over year in part due to greater female representation in senior roles.

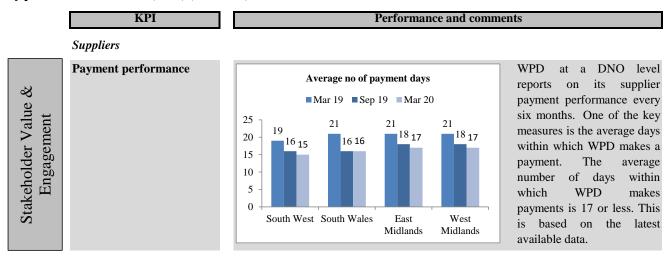
Further information about the WPD gender pay gap could be found at: <a href="https://www.westernpower.co.uk/about-us">https://www.westernpower.co.uk/about-us</a>

#### Other measures

#### - Employee satisfaction

WPD's employee survey for 2019 was reviewed and revised. This was the first year that the survey was completed online. The revised survey resulted in a move from 11 questions to 53 questions, which were subdivided into 14 distinct categories. The response to the survey increased to 51% of employees, which was an improvement of 15% in previous response rates, and it highlighted 12 key suggestions spanning across five core areas of focus i.e. opportunities for providing feedback, training and development, quality of internal communications, achieving a "thank you" culture and evidencing actions as a result of the survey. In addition to the opportunities that the survey has highlighted, almost 90% of respondents confirmed that they planned on staying with WPD for the next 12 months.

#### Key performance indicators (KPIs) (continued)



#### Response to Coronavirus

On 11 March 2020, the World Health Organisation declared the outbreak of Coronavirus ("COVID-19") a pandemic. The COVID-19 crisis has presented unprecedented challenging times and the role that WPD plays in keeping the lights on for customers has never been more crucial. At this time of uncertainty, we have continued to work 24/7 to keep power flowing to our 7.9million customers across our region, ensuring vital energy reaches homes, hospitals, factories, super markets and other essential services.

We have had to change the way we work in response to the outbreak but as always, our top priority remains the safety of our colleagues and the communities we serve. Throughout all phases of restrictions we have followed all Government guidance on safety and social distancing, whilst ensuring that our customers can continue to rely on us to provide a safe and secure electricity supply. Our ability to adapt and respond as we reasonably can coupled with a great 'can-do' attitude across WPD, has allowed us to work in many differing ways to the norm.

#### Supporting our staff

During these challenging times the health and safety of our staff has been of paramount importance.

In the weeks prior to the UK restrictions, WPD rapidly deployed its incident response procedures to ensure that sufficient laptops and other home working devices were acquired and made available to all staff and the IT team worked around the clock to get all home working technology, including networks capacities, up and running.

Quick actions were taken to secure, build and utilise IT equipment and network capacity within WPD to ensure that the majority of our office based staff could commence operating from home immediately.

For a small number of staff that are required to work from our offices, hygiene protocols have been increased. The procurement team ensured that adequate personal protective equipment ("PPE") was made available to our operational workforce. Additional vehicles were hired and new vehicles were utilised to enable staff to socially distance.

Detailed guidance have been issued and made available for employees on all relevant topics of health & safety, social distancing and home working arrangements.

Since restrictions commenced, regular updates from the CEO have taken place, providing information on the actions taken by WPD, updates on government guidelines and our plans going forward. In these updates, the CEO has urged employees to discuss and raise any concerns with their supervisors and managers and to make use of WPD's external support agencies such as the Employee Assistance Program, to enable WPD to help and support its employees in every possible way. The CEO also encouraged the staff to contact him directly for any questions, comments or suggestions.

As part of our overall planning to ensure a secure, safe and continual service to our customers, and with consideration of economic factors, the decision was taken to retain our existing staffing levels and not implement any furlough or redundancy arrangements.

WPD continues to consult with trade union and staff representatives to ensure that all staff concerns are being fully captured and addressed. As WPD considers the longer term and charts its path to the 'new normal', staff will be involved in conversations on future working arrangements.

#### Establishing a network of support

Our 'In This Together – Community Matters' fund was launched to support those hit hardest by the coronavirus outbreak. The £750,000 fund is helping local organisations to deliver support and services to the most vulnerable in our communities. For further details on this refer to our website:

http://www.westernpower.co.uk/customers-and-community/in-this-together-community-matters-fund

For the year ended 31 March 2020

#### Response to Coronavirus (continued)

#### Establishing a network of support (continued)

We are also providing additional support to the customers on our Priority Services Register ("PSR"), many of whom may find it difficult to cope with a power cut or are medically dependent on electricity. During the crisis, we are working closely with local community partners to help PSR customers most in need to access services such as food and prescription deliveries, telephone calls to combat loneliness and advice on energy savings.

We have also emailed more than 330,000 PSR customers to inform them about the help and resources we can offer during the coronavirus outbreak. A special coronavirus information portal for PSR customers has been created on our website which includes everything from energy saving tips to home schooling resources and regularly-updated frequently asked questions.

In light of coronavirus, our work to alleviate fuel poverty has also been stepped up to help households manage the financial impact of the pandemic, largely as a result of increased utility and grocery bills. Alongside our community partners, we're helping those who have been most affected by the crisis to access support and advice, including help with arranging online shopping, food bank referrals and advice on energy payments schemes.

#### Joining the fight against COVID-19

WPD has joined forces with agencies across its regions to be part of the UK's effort to combat coronavirus. This includes rapid installation of new connections at several sites, including NHS properties, in response to demands for increased electrical capacity. Our teams pulled out all the stops to complete one emergency connection in less than 48 hours.

We have also been doing a lot of work behind the scenes to ensure the resilience of electricity supplies at new and existing hospital locations, as well as to safeguard other essential services such as care homes, factories and other utilities.

#### **Future developments**

The directors consider the following areas of most significance in the short to medium term:

#### Transition to DSO

In recent years the energy sector has seen significant change, including the rapid growth of intermittent renewable generation, new technologies connecting to the distribution network and changes in the energy demands of consumers. To accommodate these changes cost effectively, our network needs to become smarter and more flexible by transitioning from the passive role of a DNO to an active role of a DSO using innovative solutions in order to mitigate the need for higher cost network reinforcement. The change from a DNO to a DSO is essential to driving performance and efficiency from our network and to ensure it can meet the future energy demands of all our customers. A DSO securely operates and develops an active distribution system comprising networks, demand generation and other flexible distributed energy resources. It is basically a smarter approach to a DNO. A DSO has greater visibility and control of assets on its distribution systems, enabling it to get the most from its existing electrical infrastructure by contracting services from distribution energy resources. In this way, a costly network reinforcement and traditional redundancy-based model of energy systems can be avoided.

As a DSO we will operate the network more flexibly, balancing sources of supply and demand in real time and avoiding, where possible, the need for costly reinforcement of the network by locally managing generation output, load and power flows. We will also facilitate better, whole system outcomes by ensuring customers can provide services up to the transmission system operator, which may avoid the need for transmission reinforcement.

In 2017 we published our DSO strategy and invited extensive feedback on it from a wide range of stakeholders including customer groups, industry and local enterprise partnerships; ensuring that our vision is aligned with the needs and priorities of our customers and partners. Having collated and analysed the responses to our consultation, we revised our strategy in December 2017, ensuring our next steps as we transition to a DSO are in line with customer and stakeholder expectations.

We are in the process of implementing our DSO strategy and have taken a range of actions, including issuing a DSO Framework which assesses the technical issues associated with the transition. In June 2019, we also issued a DSO forward plan, which provides a road map for implementation and discusses key areas pertaining to transition. In addition we have undertaken studies to assess the potential growth in distributed generation and demand and consulted with stakeholders on the potential scale of growth of energy storage. We will roll out our DSO strategy across our entire network area, prioritising those areas which will have the greatest impact, incrementally upgrading the rest of the network as customer need dictates. This transition will build on our existing innovation programme that develops and tests new solutions before deploying them as business as usual. We have developed significant competences in a number of key areas which will assist with our transition to a DSO.

Details on our DSO Strategy can be found at the link below:

https://www.westernpower.co.uk/dso-strategy

For the year ended 31 March 2020

#### **Future developments (continued)**

#### Transition to DSO (continued)

The priorities for DSO transition are also reflected within our connections activities as detailed within our work plan for the Incentive on Connections Engagement ("ICE"), which can be found at the link below:

www.westernpower.co.uk/Connections/ICE.aspx

#### Low carbon networks/Network innovation competition (research activities)

As part of the previous distribution price control period (known as DPCR5), Ofgem introduced the Low Carbon Network Fund ("LCNF"). It was set up to encourage DNOs to test new technology and commercial arrangements to support the UK's low carbon transition and climate change objectives.

The RIIO-ED1 innovation mechanisms came into force in 2015, introducing the Network Innovation Allowance ("NIA") and Network Innovation Competition ("NIC"). NIC has a similar focus to LCNF in testing technology and commercial arrangements to support the UK's low carbon transition. NIA has a broader remit encouraging technical and commercial innovation to support all DNO activities.

LCNF projects awarded during DPCR5 continue to be delivered during RIIO-ED1. Project delivery and reporting are set out in special licence conditions and in Ofgem's LCNF, NIA and NIC governance documents.

WPD has registered 68 projects under NIA covering a broad range of topics. Further details of innovation activities can be found at the link below:

www.westernpower.co.uk/innovation

#### RIIO-ED2

The RIIO-ED2 price control period commences from 1 April 2023. Ofgem consulted on the RIIO-2 framework early in 2018, and published its decision on 30 July 2018. The proposed changes applicable to all RIIO-2 price controls include:

- Giving consumers a stronger voice in setting outputs by introducing a new enhanced engagement model for RIIO-2. This involves the establishment of Customer Engagement and User Groups at company level and establishing an Ofgem-led central RIIO-2 Challenge Group;
- Allowing DNOs to earn returns that are fair and represent good value for consumers, properly reflecting the risks faced in these businesses, and prevailing financial market conditions;
- Setting the default length of the price control to five years;
- Using the regulatory framework, or competition where appropriate, to drive innovation and efficiency;
- Simplifying the price controls by focusing on items of greatest value to consumers.

In the year 2018/19, WPD set up the required customer engagement group ("CEG") and, in April 2019, the on boarding sessions of the CEG were conducted. The CEG is independent and will scrutinise the process by which our business plan for RIIO-ED2 is put together to ensure we have factored in the needs of our customers and wider stakeholders. The CEG has the ability to challenge us on various areas such as our priorities, proposed outputs and expenditure; our approach to sustainability, resilience and innovation; our transition to DSO; stakeholder engagement process; and vulnerable customer strategies. Through its independent report to Ofgem, the CEG will assist Ofgem and our stakeholders to understand whether our plans reflect the needs of our customers today and in the future.

The RIIO-ED2 strategy consultation will be launched by Ofgem in mid-2020 with a decision in late 2020. This will form the basis of WPD's RIIO-ED2 business plan. Ofgem will publish its RIIO-ED2 draft determination in June 2022 and the final determination in November 2022.

Our RIIO-ED2 stakeholder engagement plan details are available at the link below: <a href="https://www.westernpower.co.uk/introduction-and-our-riio-ed2-engagement-plan">https://www.westernpower.co.uk/introduction-and-our-riio-ed2-engagement-plan</a>

#### Risk management and controls

WPD is exposed to various risks in the ordinary course of business that may have an adverse impact on the Group's operations and financial position, thus all such risks require appropriate management. The WPD Board oversees risk management and internal control systems, and monitors the Group's risk appetite in pursuing its strategic goals. It is the responsibility of the Board to ensure alignment of strategy and risk. The emerging risk register, containing the main risks currently facing the Group, is reported to the directors monthly.

WPD's processes and systems are continually evolving alongside the needs of the business and all Group policies are reviewed by the business owners on regular basis to ensure that they are relevant to the changing landscape of the business and industry practice.

For the year ended 31 March 2020

#### Risk management and controls (continued)

In addition to appropriate policies and processes, WPD considers involvement of qualified and competent employees with the appropriate level of expertise throughout the business, a key factor for implementing an effective internal control environment.

The system of internal controls is assessed with regard to effective design and operation by the independent Internal Audit function. The Internal Audit Charter, defining the purpose, mission and responsibilities of the Internal Audit function, has been approved by the Board and the Board is responsible for:

- Approving the annual audit plan;
- Reviewing the audit results; and
- Ensuring implementation of Internal Audit recommendations.

As WPD is owned by a US publicly quoted company, it is subject to the requirements of the US Sarbanes-Oxley Act of 2002 (the "Act"). In accordance with the requirements of the Act, WPD's management undertakes an annual assessment of internal controls over financial reporting. This includes ensuring all key financial processes have been documented with specific details on the controls in place. Also a self-certification process is in place whereby senior managers affirm quarterly that disclosure controls are operating effectively and that all material information is disclosed in the financial reports. Key controls are reviewed and tested by the WPD Internal Audit team. Some of the controls in place to satisfy the Act apply to the processes that underpin the IFRS books and records.

The Board is satisfied that there is an appropriate approach to risk management and adequate and effective controls are in operation.

As WPD endeavours to achieve its goals, it considers the following risk categories most significant:

#### Goal Risk

#### On site accidents:

#### Due to the nature of the business there is an inherent safety risk associated with unsafe working practices.

#### Mitigating actions

- WPD has robust safety policies and procedures in place to ensure a safe working environment. There is a system for reporting near misses and incidents, and policies are reviewed and amended accordingly to avoid any future recurrence.
- The safety team actively supports managers with their safety responsibilities and provides assistance to enable them to maintain a clear focus on safety. During the Autumn of 2019 the safety team provided a package of presentations to support managers throughout WPD as part of the '2019 WPD Safety Week' programme. The package included an update for staff on the Group's health and safety statistics, an update on the actions following the Company Climate Safety Survey, an introduction to a new application to assist lone workers, a demonstration on how to view safety related videos on a new safety media site and a reminder about good housekeeping on site and in vehicles and offices.
- Regular safety site visits are undertaken to ensure that all safety policies and procedures are being followed and implemented. Site safety visits undertaken during the year were 9,804 versus a target of 6,003.

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#### **Network disruptions:**

Events such as weather conditions, third party damage etc. may cause disruptions, which in turn can impact results both directly through the timing of recovery relating to lower units delivered on which income is charged, and also through the system of penalties and rewards that Ofgem has in place relating to customer service levels.

- WPD has comprehensive emergency plans for network emergencies such as Black Start. Black Start is the recovery from a partial or country wide loss of electricity supply. WPD sits on a number of nationwide industry groups, along with Government Departments ("BEIS") and Ofgem to prepare for such events. These groups facilitate a consistent approach to resilience and response to network emergencies across the industry.

WPD has regular training sessions with its Network Control Centre Engineers to exercise a response to a Black Start.

- Established restoration plans are in place and reviewed with the National Grid and contracted Power Stations.
- Area operational teams undertake desktop exercises to ensure local resilience plans are appropriate.
- Considerable sums are spent on routine maintenance for network assets including tree cutting costs. Assets are managed to an accredited asset management standard, ISO55001, to support the right decision making with respect to asset maintenance and replacement.
- In addition to normal equipment stocks, WPD also keeps a small number of additional strategic spares and is part of the National Grid strategic spares group.
- WPD has a resilient IT infrastructure with multi-site running with fault tolerant/mirrored systems.
- Flood plans are in place for major substations.
- There are reciprocal arrangements in place with other network operators for backup support through NEWSAC (North East West South Area Consortium).

# Network Performance & Security

#### Risk management and controls (continued)

#### Goal

Network Performance & Security

#### Risk

#### Mitigating actions

### Cyber breach threat:

Unauthorised access to our key networks and systems.

- Stringent policies and procedures are in place to provide controls around network security, proactive threat intelligence gathering, asset management, data backups and incident response.
- A dedicated and qualified team is in place, that continually reviews and monitors our cyber security position and reporting capabilities.
- WPD limits direct connection of WPD's corporate network to the internet, direct cloud based services and personal devices.
- All data considered to be 'in transit' is secured using a variety of methods and techniques including Hypertext Transfer Protocol Secure ("HTTPS"), Secure File Transfer Protocol ("SFTP") and Lightweight Directory Access Protocol ("LDAP").
- Regular security drills are performed involving the Information Resources department and business teams.
- All servers are backed up for both operational and disaster recovery purposes and the data is secured off-site. This facilitates full recovery of each system, once the appropriate replacement hardware, or hosting capacity, has been sourced. Disaster recovery testing is performed on a regular basis.
- Extra measures have been put in place due to the heightened risk from Coronavirus ("COVID-19"), relating to a high number of employees working from home. Users have been advised of security measures to follow when using WPD assets from home, along with guidance to ensure the safe use of video conference facilities. Extra monitoring controls have been implemented around the Group's externally facing systems and the Group's VPN/RDP connections. We have also conducted additional penetration tests and vulnerability scans to ensure our external connections remain secure, and reviewed our incident response procedures relating to our internet infrastructure.
- WPD took part in a national level cyber security exercise organised by the Government, which raised awareness about the threat of cyber security attacks and gave us an opportunity to enhance our "continued improvement" cyber security programme.

#### **Interest rate risk:**

WPD has had both shortterm and long-term external debt during the year, at floating and fixed rates of interest, which exposes it to interest rate risk.

- WPD's interest rate risk management policy seeks to achieve the lowest possible cost of debt financing, while managing volatility of interest rates, applying a prudent mix of fixed and floating debt, either directly or through the use of derivative financial instruments affecting a shift in interest rate exposures between fixed and floating, and also matching debt service requirements to projected cash flows.
- An element of the long-term debt is index linked which creates a natural hedge against WPD's regulated income, which is also index linked.
- WPD also uses forward-starting interest rate swaps to minimise exposure to cash flow interest rate risk for any future planned issuance of debt.

#### Credit risk:

A customer or counterparty to a financial instrument will fail to perform and pay the amount due causing financial loss to the WPD Group.

- WPD is exposed to credit risk on its billed and unbilled portion of customer contributions in relation to any capital work undertaken. WPD maintains credit policies and procedures with respect to counterparties. Depending on the creditworthiness of the counterparty, WPD may require collateral or other credit enhancements such as cash deposits or letters of credit and parent company guarantees.
- WPD has minimal credit risk in relation to debtors pertaining to revenue from providing distribution use of system services ("DUoS"). DUoS debtors are protected by Ofgem regulations, provided credit management for these receivables is performed in accordance with industry standards as set out by Ofgem and governed by the Distribution and Connection Use of System Agreement ("DCUSA").

#### Exchange rate risk:

Negative currency fluctuations on foreign currency denominated debt.

Where long-term debt is denominated in a currency which is not sterling, the WPD Group's policy is to hedge exposure to fluctuations in exchange rates through cross-currency swaps.

# Financial Stability

#### Risk management and controls (continued)

#### Goal

#### Risk

#### Mitigating actions

Financial Stability

#### **Inflation risk:**

The WPD Group's indexlinked borrowings and interest liabilities are exposed to a risk of change in the carrying value due to changes in the UK RPI.

The WPD Group's regulated assets ("RAV") are linked to RPI due to the price setting mechanism imposed by the regulator, and also the allowed revenue is linked to RPI. By matching liabilities to assets, index-linked debt naturally hedges the exposure to changes in RPI and delivers a cash flow benefit, as compensation for the inflation risk is provided through adjustment to the principal rather than in cash.

### **Impact of Brexit:**

The European Union referendum vote on 23 June 2016 has resulted in considerable uncertainty for UK businesses.

Following the European Union referendum vote on 23 June 2016, the UK formally left the EU on 31 January 2020. Under the withdrawal agreement the transition period commenced and is scheduled to end on 31 December 2020. As the UK continues to negotiate trade agreements, there is continued uncertainty in connection with access to the EU market after the end of the transition period. There is a potential risk of supply chain disruption including inventory shortages due to restrictions between UK and EU borders after the end of transition period. In response to this risk, management has identified, and ordered in bulk, critical stocks that merit stockpiling and has taken steps to secure additional storage on site facilities or at UK based suppliers.

Uncertainty around Brexit has resulted in the weakening of sterling; however WPD's revenues and assets are principally sterling denominated, thus minimising any foreign currency risk for WPD. Any foreign currency debt is fully hedged by cross currency swaps. Nevertheless the Company will continue to monitor the implications of Brexit on its operations throughout the transition period.

#### **Regulatory changes:**

Changes in legislation relating to environmental and other matters are not adopted by WPD.

- WPD has a dedicated regulation and compliance department with skilled personnel that track any regulatory changes and provides advice in relation to interpretation and compliance of those changes.
- There is regular engagement with the WPD Board on political and regulatory developments which may impact the Group. The Board monitors management's progress in ensuring compliance with changes to legislation.

#### **Negative** impact of network assets on the environment:

Due to the nature of equipment used in the industry, network assets may have a harmful impact on the environment.

- Use of best technology to minimise the impact of network assets on the environment, such as the use of Perfluorocarbon Trace ("PFT") technology within WPD, reduces the effect on the total annual fluid losses.
- Frequent assessment and careful monitoring of all its network assets, specifically assets like SF6 equipment, which produce SF6 gas linked to potential global warming. WPD carefully monitors its SF6 equipment and employs the external ENA Engineering Recommendations for the reporting of SF6 banks, emissions and recoveries.
- Following best practices and complying with various guidelines in connection with environmental practices such as:
- a) G92/1 Guidelines for best practice in relation to Electric and Magnetic Fields ("EMFs") in the Design and Management of Low Voltage Distribution Network,
- b) BEIS Code of Practice on the Optimal Phasing of High Voltage Double Circuit Power.
- c) WPD complies with the public exposure recommendations contained within the 1989 ICNIRP (International Commission on Non-ionising Radiation Protection) Guidelines on Extremely Low Frequency Electromagnetic Fields,
- d) Occupational exposure requirements specified within the Control of Electromagnetic Fields of Work Regulations 2016.

# Environment

#### Goal

#### Risk

#### Mitigating actions

# Customer dissatisfaction:

Failure to meet the required level of customer satisfaction performance.

- WPD's Customer Collaboration Panel ("CCP") meets quarterly and expert members represent a wide range of customers and other key stakeholder groups. Through the panel, we proactively seek honest and challenging customer views about the way we operate and our future plans. The CCP critically reviews our performance and, through extensive expert knowledge, provides strategic steer on our short and long term priorities. Members provide an external view to our business, acting as a sounding board for new ideas and initiatives as well as collaborating with WPD to create and influence future policy and processes.
- Our Customer Engagement Group ("CEG") was established as part of RIIO-ED2's enhanced engagement. WPD was the first DNO to set up a new CEG a group of 15 members who scrutinise our Business Plan and provide assurance to Ofgem that the plan and the engagement used to create it are robust.
- Annually WPD hosts workshops to gather stakeholder insight which shapes the direction of our business, by allowing stakeholders to set our priorities now, and for the future. In 2019 a record 330 stakeholders from a range of different backgrounds (including domestic, business, local authorities, developers, environmental, energy/utility, regulatory/government and voluntary sectors) attended six workshops. Improvement actions are identified as a result of the workshops and are subsequently addressed and delivered by WPD. An online portal means stakeholders who cannot attend can view content and videos and take part in the consultations.

# Lack of skilled employees:

Failure to attract, retain and to develop our employees.

- WPD maintains good practices and safe working conditions.
- WPD's employees have access to pension schemes (Contribution schemes for the new members).
- WPD has benchmarked terms and conditions for all employees.
- Employees are kept informed of WPD's goals, objectives, performance and plans, and their effect on them as employees, through monthly business updates, regular team briefings, as well as through WPD's in-house journal. Formal meetings are held regularly between senior managers and representatives of staff and their unions to discuss matters of common interest.
- A series of roadshow presentations by the directors is conducted each year to ensure that all staff are aware of, and can contribute to, WPD's goals.
- Various training programmes are offered under the Trainee Development Scheme and Technical Apprentice Scheme.
- Succession plans are in place for key roles within the organisation.

#### **Reliance on suppliers:**

WPD relies on a limited number of suppliers for cable laying and tree cutting services, and for the supply of cables, plant and machinery.

- There are sufficient alternative suppliers for cable laying, tree cutting etc. such that, should an existing supplier be unable to continue to make supplies, there will be no significant long-term impact on WPD's ability to operate the network.
- Most of the electricity which enters WPD's network is carried on the National Grid's grid supply points and thus WPD is dependent on National Grid. National Grid is the electricity transmission and electricity system operator ("ESO") regulated by Ofgem and thus the risk of a major failure is considered very remote.
- All strategic contracts are regularly reviewed by the purchasing team to ensure business continuity.

#### Regulatory risk:

WPD's revenue is regulated and is subject to a review at the end of each price control period. Thus WPD is subject to a high degree of political, regulatory and legislative intervention, which can impact both the current RIIO-ED1 period, and the next RIIO-ED2.

- WPD deploys significant resources in engaging with Ofgem on all new publications.
- WPD is actively involved in the RIIO-ED2 consultations.
- WPD is evolving plans for development of RIIO-ED2 modelling, building on RIIO-ED1 work and the current annual forecasting process.
- WPD engages with its shareholder on all changes and encourages investor dialogue between PPL, its shareholders and Ofgem.

# Stakeholder Value & Engagement

For the year ended 31 March 2020

#### Risk management and controls (continued)

#### Other current risks - Coronavirus 2019

In response to the COVID-19 pandemic, globally, governments had to take a variety of extensive actions to contain the spread of the virus including quarantines, stay-at-home orders, travel restrictions, reduced operations or closures of businesses, schools and government agencies and legislative or regulatory actions to address health or pandemic related concerns. The spread of the virus and the measures to contain it have disrupted the world economies and presented extraordinary challenges to businesses, communities, workforces and markets.

The Group has performed a detailed risk assessment of the current and future impacts of COVID-19. As at 31 March 2020 there has been no material impact on the Group's business, results of operations, financial condition, liquidity or on its supply chain as a result of COVID-19.

WPD is a Category 2 Responder under the Civil Contingencies Act 2004 and has been designated as a Key Worker under the UK Government's plans to keep the country operating during the COVID-19 pandemic. WPD continued to work according to government guidelines, including undertaking appropriate social distancing measures, whilst continuing to provide a safe, secure and reliable supply of energy to our customers

Following the announcement of restrictions in the UK, operational works initially focused on essential activities only, with an ongoing review of and changes to what activities that includes, at both government and regulatory levels. This included fault restoration and repair work, as well as activities of a safety critical nature and critical connection work in support of the response to the COVID-19 pandemic (e.g. connections to care homes, hospitals and other health care facilities, food shops and wholesalers, food production, telecoms and broadband). This approach has been subject to review following UK Government and industry regulator updates; as at July 2020 the Group has resumed operations in relation to non-safety critical capital programmes, subject to appropriate safety measures. Thus during these unprecedented times, where many business sectors are impacted severely, WPD has a continuing licence obligation to be a sustainable business and to continue to provide essential services to our customers.

Subsequent to the year ended 31 March 2020, revenues have been impacted temporarily due to reduced load demand from industrial and commercial customers, slightly offset by increased demand from domestic customers as a direct result of businesses and the public adhering to government restrictions. Any impact on revenue is largely a timing issue due to the regulatory regime that ensures that allowed revenue under a price control period is recovered in future years.

The Group has not experienced a significant reduction in cash receipts subsequent to the year ended 31 March 2020 and therefore has not adjusted the allowance for uncollectable accounts for potential additional expected credit losses as at 31 March 2020.

The forecast future net cash flows of the Group have not been impacted materially due to the pandemic. The impact due to the temporary decline in revenue has been offset by a temporary decline in the capital work programme of the Group. WPD does not anticipate any liquidity issues as it has access to sufficient capital as and when required. The details of this can be found in the Directors' report (page 32) and notes to the financial statements (page 85).

The Group has sufficient stock levels of critical inventory and does not anticipate any shortage of supplies in the near future. The Group continues to actively review and monitor its supply chain to identify early any shortages or gaps.

Due to volatility in the financial markets, businesses are facing increased foreign currency risk. WPD's revenues and assets are principally sterling denominated, thus minimising any potential foreign currency risk exposure. Any foreign currency debt is fully hedged by cross currency swaps. Nevertheless, the Group continues to monitor the implications of exchange rate movements on its operations.

In the preparation of these financial statements, certain key estimates and assumptions are made to arrive at the carrying value of assets and liabilities recorded. An impact assessment has been undertaken of the COVID-19 pandemic on key estimates and assumptions of the Group as at 31 March 2020, particularly in relation to pension measurements and goodwill impairment. Details can be found in note 2 of the financial statements on page 62.

#### Corporate and social responsibility

We care about our customers and our communities, the way we interact with our stakeholders and how we take responsibility within the communities we serve.

#### Social and community

Working with our communities is important in creating shared value for us as a business, the people we serve and the communities we operate in.

For the year ended 31 March 2020

#### Corporate and social responsibility (continued)

#### Social and community (continued)

In the year to March 2020, WPD assisted 276 (2019: 306) separate charitable and non-charitable organisations as part of a £259,000 (2019: £284,000) commitment - this included bursary support for underprivileged children involved with Duke of Edinburgh awards, a British Heart Foundation initiative to provide CPR kits in schools and Wildlife Trust partnerships in Bath and Gloucester.

While maintaining these core themes, we have also continued to tailor our support to align, where appropriate, with the feedback from our stakeholders and customer opinion research from our customer awareness activity. With regard to its customer groups WPD has launched the following activities:

#### - Vulnerable customers

WPD is required to hold a Priority Services Register ("PSR") that records details about vulnerable customers so that additional support can be provided when the customer contacts WPD or when their supply is interrupted. Specifically help is provided for vulnerable customers during power cuts and where possible advice is provided to enable them to be prepared should a power cut occur

WPD has established a dedicated team of people to proactively contact customers and check the detail held about them. This is a process that will be repeated every two years to ensure that the register remains up to date. WPD is also developing processes to share data with other service centred organisations that hold information about vulnerable customers, in line with data protection laws. Links have been established with many organisations such as the British Red Cross to improve the understanding of the needs of vulnerable customers. These partners work with WPD to improve the services that are provided and we will continue to work with them.

#### - Fuel poverty and energy affordability

Some customers on low incomes cannot afford to effectively heat their properties. Whilst WPD does not have a direct obligation to provide energy efficiency advice/support, in 2013 we introduced a social obligations strategy that is updated and reviewed by our Chief Executive annually and includes actions WPD will take to address fuel poverty by helping customers to access information and key support. In recent years we have worked with expert partners such as the Centre for Sustainable Energy, Citizens Advice and with the Energy Saving Trust to provide information for our customers on the causes of and solutions for fuel poverty.

WPD has been working with four charitable organisations, one in each of our licence areas, to deliver an innovative fuel poverty referral scheme called 'Power Up'. The project helps customers by offering income and energy efficiency advice, such as benefits and tariffs advice and energy saving schemes. Based on feedback from our Customer Panel customers are offered free, independent, confidential and impartial advice on various measures. The project works by partner organisations such as Citizens Advice taking referrals directly from WPD. Every customer contacted as part of WPD's PSR data cleanse is given the opportunity to be referred to a partner organisation, such as Citizens Advice and the Centre for Sustainable Energy, for support.

In addition our 'Affordable Warmth' schemes work in a similar way but for customers not already known to us. Partner organisations help us identify hard-to-reach fuel poor customers and they provide the same support as detailed above and then refer customers to WPD's PSR.

In 2019/20, these projects supported over 18,000 (2019: 16,000) fuel poor customers across WPD, leading to estimated annual savings of £10m (2019: £6m) for these customers.

Details on our priority services can be found at:

https://www.westernpower.co.uk/customers-and-community/priority-services

#### - Deaf awareness chartermark

WPD holds the Action on Hearing Loss (formerly RNID) 'Louder Than Words' charter mark accreditation, which assesses and endorses the accessibility of WPD's services for deaf and hard of hearing people. We have held the accreditation for eight and ten years respectively for WPD South Wales/WPD South West and WPD East Midlands/WPD West Midlands. We are the first DNO in the UK to have launched the "InterpreterNow" service. This enables deaf customers to contact us in British Sign Language ("BSL") via an online interpreter by downloading a free app. In addition, we now provide a series of customer information videos in BSL.

#### Taxation

WPD is committed to comply fully with the UK tax legislation and endeavours to pay the right amount of tax at the right time, taking a prudent approach where there is any uncertainty. WPD does not engage in any aggressive or artificial tax planning to reduce its tax liabilities. WPD values an open working relationship with HM Revenue & Customs and keeps it aware of any major business developments. The WPD Board takes ultimate responsibility for the management of taxation affairs in the UK, including the management of risk, the compliance process and the control environment in which the tax department works. For details of the Group's effective tax rate see note 10.

For the year ended 31 March 2020

#### Corporate and social responsibility (continued)

#### Taxation (continued)

For our tax strategy refer to the link below:

https://www.westernpower.co.uk/about-us/financial-information

#### Human rights

WPD is dedicated to conducting its business with honesty, integrity and fairness. In support of these principles, it is WPD's policy to observe all domestic and applicable foreign laws and regulations including the Human Rights Act 1998, Equality Act 2010 and Modern Slavery Act 2015. Annual training of all employees is conducted in relation to these laws and regulations, which has led to an understanding within the Group of issues associated with these statutes. The outcome of our policies and procedures is that there have been no known instances of any form of discrimination, slavery or human rights violation.

For our Modern Slavery Act 2015 statements refer to the link below:

https://www.westernpower.co.uk/modern-slavery-act

#### Anti-corruption and anti-bribery

WPD has robust policies on anti-corruption and anti-bribery. These policies apply to all employees of the Group and form part of the employee Code of Conduct. Other individuals performing functions for the Group, such as agency workers and contractors, are also required to adhere to our anti-bribery and anti-corruption policies. Through our policies and procedures, we have been able to foster an environment of zero tolerance towards bribery and corruption. As a result there has been no known violation of applicable laws and policies.

#### Non-financial information statement

In accordance with section 414CB of the Companies Act 2006 we have reported on various non financial information as follows:

#### - Business model

Refer to page 1.

#### - Environment

Refer to page 3 for details on our policy regarding the environment.

Refer to pages 8 and 9 for details of the impact of our activities on the environment and our performance in this area.

Refer to page 16 for our principal risks in relation to the environment and our actions to mitigate those risks.

#### - Employees

Refer to page 4 for details on our policies regarding employees.

Refer to page 10 for our performance in relation to employee satisfaction.

Refer to page 17 for our principal risk in relation to employees and our actions to mitigate that risk.

#### - Social matters

Refer to pages 18 and 19 in relation to details on our policies and activities in relation to our social responsibilities.

#### - Human rights

Refer above.

#### - Anti-corruption and anti-bribery matters

Refer above.

#### **Section 172 Statement**

Refer to pages 27 to 30 for our Section 172 statement.

By Order of the Board

P Swift

Chief Executive

23 July 2020

#### **Western Power Distribution plc**

Avonbank

Feeder Road

Bristol BS2 0TB

#### Corporate governance statement

For the year ended 31 March 2020

For the year ended 31 March 2020, under The Companies (Miscellaneous Reporting) Regulations 2018, Western Power Distribution ("WPD") has adopted the Wates Corporate Governance Principles for Large Private Companies.

The principles below have been applied throughout the year ended 31 March 2020.

#### Purpose and leadership

Our core business is to provide safe and reliable electricity supplies to our 7.9 million customers who rely on us each and every day. The service we provide is critical to the lives and livelihoods of the communities that we serve. Our primary purpose is to provide industry leading maintenance, protection and development of our critical energy infrastructure assets to deliver safe and secure networks that meet the needs of our current and future customers. We strive to fulfil our purpose with the highest regard to the safety of all involved and to deliver the best possible service for our customers and stakeholders in an environmentally sustainable manner.

The culture within WPD is driven by our Board, which is made up of a team with extensive experience of both the energy sector and the customer focused values that have long been the cornerstone of WPD's sector leading service delivery. The Board strives to encourage the workforce to take personal ownership by following the golden rule: "treat the customers the way you would like to be treated".

The Board values strong relationships with all stakeholder groups and oversees a comprehensive programme of engagement with our stakeholders to ensure that our business strategies and values are aligned. For further information please refer to our strategy and key goals as detailed in our Strategic report on pages 2 to 5.

Our Board recognises the important contribution made by all employees in delivering our purpose. Our vision and values are communicated to employees through annual roadshows presented by the Chief Executive and supported by the executive directors. These values are reinforced to all employees through our annual objective setting and performance review process. Additionally, in the current year, the Board conducted a Leadership Conference presented by the Chief Executive and Board members to the senior management team of the Group. This initiative helps to strengthen our values and supports open dialogue between the executive and senior management team and thus key messages communicated by the executive directors are cascaded throughout the organisation.

Our in-house magazine and regular news bulletins support the delivery of our purpose and values across the organisation, communicating examples of our values and illustrating positive behaviours.

The Board utilises annual staff opinion surveys as a key tool of assessing the effectiveness of communication and engagement across the workforce. These measure a range of factors impacting staff, for example a safety survey steered by the Chief Executive sought to obtain safety perceptions, values and behaviours across the workforce. The knowledge attained has been used to evaluate the safety environment of the Group and to identify both best practice and areas of improvement, with the results being shared across the organisation.

The Board strives to support a customer centric ethos whereby staff are empowered to take personal responsibility to continuously ensure the provision of excellent service. As a result of this vision being reinforced by the executive directors and the senior management team, outstanding customer service is a binding ethos throughout WPD's workforce. Strategic decisions on the business model and organisational structure underpin this ethos, for example placing our operational staff and resources geographically close to the communities they serve.

The Board welcomes and invites feedback; it also recognises that staff may wish to raise concerns anonymously. An ethics helpline provides employees with the opportunity to report any concerns. A defined policy is in place for resolution of any concern reported through the helpline.

The Board is committed to fostering an effective relationship with its single shareholder, PPL, and actively promotes engagement and transparency to ensure that the values within the Group are aligned to investor priorities.

#### **Board composition**

The WPD plc Board comprises four executive directors and five non-executive directors. The non-executive directors are part of the senior management team of the WPD Group shareholder, PPL. See page 1 of the Strategic report for details on ownership.

The designation of the executive director roles are Chief Executive, Operations Director, Finance Director and Resources & External Affairs Director. All the executive directors are experienced in their respective roles and responsibilities.

Key functions of the business are reflected within the organisational structure of the Group and fall within three broad areas i.e. operations/logistics, resources and external affairs and finance/IT. The size of the Board is aligned to the organisational structure of the Group with each executive director responsible for the oversight of its relevant area under the common leadership of the Chief Executive.

For the year ended 31 March 2020

#### **Board composition (continued)**

Independent oversight responsibilities lie with the non-executive directors. The non-executive directors possess the necessary skills and experience of the utility sector and wider business sectors to provide oversight of the Company. In fulfilment of their duties they have access to the Company Secretary and to legal advisors funded by the WPD Group. As with all Board members the non-executive directors have the authority to request Board meetings.

All directors, including the Chief Executive, have equal voting rights when making Board decisions.

The Chief Executive is appointed by the Group shareholder, PPL. The Governance and Nominating Committee ("GNC") of PPL seeks candidates with a broad range of demonstrable abilities and accomplishments beyond that of corporate leadership. These abilities include sufficient skills and expertise to provide sound and prudent guidance in respect of the Company's operations and interests. When making appointments, the GNC takes into consideration skills, expertise, background, professional experience, education, and a variety of other attributes that contribute to the Board's collective strength. Further a separate committee of PPL, Compensation Committee ("CC"), is responsible for the succession planning of the Chief Executive.

Other executive directors and non-executive directors are nominated by the shareholder in consultation with the Chief Executive, and elected and formally appointed by the existing Board members. The process followed for nomination of the directors involves consideration of the relevant skills, expertise, experience, professional background and various other personal attributes.

A detailed profile of our executive team can be found on our website at the link below: <a href="https://www.westernpower.co.uk/about-us/meet-our-executive-team">https://www.westernpower.co.uk/about-us/meet-our-executive-team</a>

Newly appointed directors undertake an induction programme which is tailored to their specific needs.

The Board ensures their knowledge is current and relevant through a variety of means such as attending appropriate industry conferences, holding memberships of relevant institutes, completing technical training updates and attending meetings with various industry participants e.g. regulators, investors and banks. The executive directors adopt a hands on leadership style and regularly meet with their management teams to ensure that they are updated on the latest business developments and have immediate access to current information.

#### **Directors' responsibilities**

#### Accountability and discharge of responsibilities

There are well-defined policies, as approved by the Board, clearly establishing the overall duties and liabilities of the directors, the areas of responsibility and accountability for each director, the process for delegation of authority by the Board and the matters reserved for the Board. There is a robust process in place for the regular review and update of policies and processes to ensure they remain relevant and fit for purpose.

There are four principal Board meetings for the WPD Group each year. In addition, there are four principal DNO Board meetings each year. If the need arises, the directors can call additional meetings at any time, organised through the Company Secretary. The Board receives and is updated on all key and important business information by the executive directors at the Board meetings. The Board is supported by the Company Secretary to provide guidance on key governance requirements.

Overall operational responsibility of the WPD Group lies with the Chief Executive. The Chief Executive fulfils this responsibility in conjunction with and through oversight of the other executive directors. Regular formal meetings, known as the Executive Council, consist of the Chief Executive plus the other executive directors. This acts as a forum for the discussion of business performance, strategic considerations and identification of matters to be considered by the Board. Other senior management may attend the meetings for the purpose of providing updates to the directors. Any key items are circulated and communicated to the Board in a timely manner.

The executive directors are responsible for the organisational performance of their directorate and are accountable to the Chief Executive and the Board. Executive directors regularly meet with their respective senior management teams to discuss matters impacting the Group. Key Performance Indicator ("KPI") monitoring is delegated to senior managers who report directly to their respective executive director. While maintaining complete oversight of their area of accountability, the executive directors empower senior management to take operational decisions, apply their knowledge and utilise their industry experience in the day to day management of the business.

The executive directors understand the importance of leading with integrity. Annual training on "Standards of integrity," as endorsed by the Board, is mandatory for all staff including the executive directors. Company policy sets out potential conflicts of interest and at each Board meeting the directors disclose any potential conflicts of interest in any of the Group transactions or arrangements. In addition the Company Secretary administers an annual process, whereby the directors disclose any interests in related parties or any related party transactions.

For the year ended 31 March 2020

#### **Directors' responsibilities (continued)**

#### **Integrity of information**

At the quarterly Board meetings the Board receives information on all key aspects of the business including safety, environmental matters, risks and opportunities, financial performance, strategic and regulatory matters, operational matters, market conditions, changes in the political landscape and updates on relevant technological developments. Board information is prepared by a centralised team and is subject to detailed review procedures at various levels of senior management prior to submission to the Board.

Key financial information is taken from the Group's financial systems. Our finance team is appropriately qualified to ensure the integrity of this information and necessary training is provided to keep them up to date with statutory, regulatory and financial reporting requirements. As WPD is owned by a US publicly quoted company, it is subject to the requirements of the US Sarbanes-Oxley Act of 2002 (the "Act"). In accordance with the requirements of the Act, our management team undertakes an annual assessment of internal controls over financial reporting. This includes ensuring all key financial processes have been documented with specific details on the controls in place. Key controls over financial reporting are periodically reviewed and tested by our Internal Audit team.

Key regulatory information is prepared annually for submissions to the regulator, Ofgem. We have extensive internal data assurance and governance procedures and established policies for ensuring data integrity in respect of information submitted. Data is compiled from source systems that have appropriate validation checks and is prepared, reviewed and approved by WPD's experienced personnel.

KPI information is available to the management via the use of a dashboard. This system interfaces directly with source systems and data, and was implemented following extensive testing procedures on data accuracy.

The Board's review of the information in relation to various areas of business allows the directors to assess that systems, processes and procedures continue to operate effectively and assists in identifying and strengthening governance arrangements.

#### Opportunity and risk

#### **Opportunity**

We strive to create and preserve value over the long term by consistently providing outstanding customer service at an efficient cost by combining technical excellence and innovation within a clear organisational structure.

Within the parameters of operating within a regulated environment, the Board identifies and evaluates relevant opportunities to create long term value for the WPD Group and its stakeholders.

In June 2013, we published our Business Plan for the eight year period from April 2015 to March 2023. The business plan sets out our view of infrastructure investment requirements and aligns with Ofgem's eight year regulatory price control review, known as RIIO-ED1; the first for electricity distribution to be determined using the RIIO (Revenue = Incentives, Innovation and Outputs) framework. A key feature of the RIIO model is that setting of outputs that are expected to be delivered is more extensive and embedded within our overall business plan. Our plans and commitments within the business plan have been influenced by our stakeholders and progress towards achievement is actively monitored by the Board. During 2019/20, in addition to outperforming the majority of our RIIO-ED1 commitments, we continue to take great strides towards transitioning from DNO to Distribution System Operator ("DSO") and focusing on delivering a smarter, more flexible energy system.

Looking beyond RIIO-ED1, with proactive engagement by the directors, we have commenced conversations about our RIIO-ED2 business plan (April 2023 to March 2028) and beyond in stakeholder workshops and established a new Customer Engagement Group ("CEG") to deliver customer focused challenge on our plans. A senior manager has been appointed by the Board having responsibility to oversee and lead our RIIO-ED2 business planning process, demonstrating the directors' determination to allocate resources to key business areas creating most value for the Group and its stakeholders.

Ensuring we are prepared for and are taking account of future changes and market conditions is a key factor in delivering our long term strategy and delivering long term stakeholder value. For this purpose the Executive Council convenes an annual strategic review where strategic direction and forward looking plans for the WPD Group are discussed.

The Board is constantly engaged in considering technological advances and is invested in the development of smarter ways of working throughout the business. Publication of our DSO plan and the launching of a new brand, 'Flexible Power,' to seek market-provided sources of flexibility (which will allow us to accommodate increasing demand for electricity without having to build a larger network), are recent examples of how innovation and technology can be harnessed to create business opportunities through efficiently meeting the needs of our stakeholders. Other examples of key initiatives undertaken by the executive directors include:

For the year ended 31 March 2020

#### Opportunity and risk (continued)

#### Opportunity (continued)

- Electric vehicles ("EV") We published our EV strategy and organised EV conferences to assist local authorities in the development of plans for projected volumes of EVs.
- Smart grids The Board endorses innovation in the area of smart grids and meters so that new techniques are developed and enhanced data from smart meters is captured and utilised to help develop a more dynamic network.
- Losses management We have adopted a detailed approach to reduce technical engineering losses from the network by taking various measures which are outlined in detail on our website at the link:
  - $\underline{https://www.westernpower.co.uk/smarter-networks/losses/losses-management}$
- Climate change adaption In response to requirements set by the Department of Environment, Food and Rural Affairs ("DEFRA") and the Climate Change Act 2008, WPD has produced "Adaptation to Climate Change" reports highlighting the work being undertaken by us in this area. Reports can be found on our website at the link: <a href="https://www.westernpower.co.uk/customers-and-community/environment/carbon-impact-and-climate-change">https://www.westernpower.co.uk/customers-and-community/environment/carbon-impact-and-climate-change</a>
- Cyber security measures A qualified team has been established who are dedicated to cyber security and is one of the key measures taken by the directors to evaluate and mitigate cyber security risks. In addition, we were also one of the 170 participants that took part in a national level cyber security exercise organised by the Government, which raised awareness about the threat of cyber security attacks and gave us an opportunity to enhance our "continued improvement" cyber security programme.

#### Risk

The WPD Board oversees the risk management of the Group and develops the Group's overall risk appetite whilst in pursuit of its strategic goals. The responsibility for internal controls cascades from the Chief Executive and the executive directors to senior management teams responsible for risk assessment and the implementation of appropriate mitigation. Managers are responsible for the identification of risks and the deployment of appropriate controls within their areas of responsibility. Policies are established, reviewed regularly and made available on the Group website to assist the managers with establishing an appropriate control environment. We consider the involvement of qualified and competent employees with the appropriate level of expertise throughout the business a key factor for implementing an effective internal control environment.

Risk management is embedded into the organisational structure with specialist teams established to manage certain key risk areas. Specifically, we have long established teams reporting to senior managers responsible for health and safety, regulatory compliance, employee relations, cyber security, financial reporting and legal compliance.

An Enterprise Risk Management process is in operation with a focus on recognising emerging risks. Identification and consideration of significant and emerging risks and subsequent related decisions, if any, are undertaken by the Executive Council. The Executive Council exercises suitable judgement as to any control decisions that merit Board attention. Emerging risks are regularly reported to the Board, facilitating the oversight of the risk management process of the Group. Pages 13 to 18 of the Strategic report outline the key risks and the related mitigating actions for the WPD Group.

We have an established internal audit function reporting directly to the Chief Executive. The head of internal audit also attends and reports directly to the WPD Group Board members at their quarterly meetings. The WPD internal audit function also reports into the Audit Committee of the shareholder, PPL. The internal audit approach follows a recognised audit framework to ensure the Group is compliant with relevant legislation e.g. Sarbanes-Oxley Act 2002 (as required by our US shareholder). The Internal Audit Charter, defining the purpose, mission and responsibilities of the Internal Audit function, has been approved by the Board. The Board is also responsible for approving the annual audit plan, reviewing audit results and monitoring the implementation of Internal Audit recommendations. Regular updates, including progress of Internal Audit testing are provided to the Board.

#### Remuneration

The remuneration policy applicable to the role of Chief Executive is set by the PPL CC. The policy is reviewed annually by PPL at its Annual General Meeting and is detailed in PPL's Annual Proxy Statement. PPL's 2020 proxy statement can be found at: <a href="https://pplweb.investorroom.com/proxy">https://pplweb.investorroom.com/proxy</a>

The CC uses an independent consultant to ensure that the executive compensation programme is reasonable and consistent with competitive industry practices. The consultant reviews the remuneration policy in line with market compensation data and information on pay practices from the utility and general industry comparators. After considering the advice from the consultant, the CC arrives at compensation packages that are aligned with achievement of the PPL Group's purpose, long term and short goals that include operational and financial targets and overall strategic priorities.

Remuneration of the other executive director roles is approved by the shareholder PPL, with input from the WPD Chief Executive Officer, following the review of an internal benchmarking exercise of base salary plus long and short term incentives covering operational and financial targets. Elements of directors' remuneration is directly linked to the Group's performance targets which align to the Group's purpose and values.

For the year ended 31 March 2020

#### **Remuneration (continued)**

The remuneration of non-executive directors is determined by the shareholder, PPL.

The pay of WPD's wider workforce is consulted and agreed upon with the recognised trade unions, with the aim to ensure that the terms and conditions are aligned to current industry practices.

#### Stakeholder relations and engagement

The Board believes that the overall success of the business is dependent upon the way we work with our stakeholders and is fully committed to fostering effective stakeholder relationships that are aligned to the Group's purpose and strategy. Our key stakeholders are customers, employees, regulators, suppliers and our shareholder; the Board actively promotes engagement and transparency with all these stakeholder groups and the executive directors ensure that a fair and balanced view of the Group's position is communicated to the relevant stakeholders. This is outlined below:

#### **Customers**

We have an established customer panel that meets four times a year with members, who represent a wide range of customers and other key stakeholder groups. The panel is attended by the Chief Executive and other directors and through the panel, they seek honest and challenging customer views about the way we operate and our future plans. This level of engagement plays an important role in helping WPD achieve its purpose of delivering good value and quality service for its customers.

Annually we host workshops to understand the needs of our stakeholders so that they are aligned with the strategic priorities of the Group. The directors participate in these workshops and improvement actions identified are subsequently considered and, where appropriate, implemented.

The newly created CEG, as part of RIIO-ED2's enhanced engagement, will fulfil a vital role to ensure customers are placed at the heart of our plans for the future and that actions and decisions made by us are truly positioned to deliver in the long-term interests of customers. The CEG is independent and has the ability to challenge us on various areas such as our priorities, proposed outputs and expenditure, our approach to sustainability, resilience and innovation; our transition to DSO; the stakeholder engagement process; and vulnerable customer strategies. Recommendations from the CEG group will be reviewed and considered by the Executive Council and in turn by the Board.

The directors' commitment, and in turn that of senior management and the wider workforce, of being proactive in customer engagement is evident from the fact that WPD has maintained its position as the top performing DNO group in the Stakeholder Engagement Incentive Award Scheme (a key element of Ofgem's Broad Measure of Customer Satisfaction), since its introduction in 2011/12. In 2018/19 WPD was again rated first place in the industry (outperforming every DNO, gas and transmission network) with a score of 8.35 out of 10.

For further details on engagement with customers please refer to page 3, 4, 9, 10 and 17 of the Strategic report.

For details on engagement with vulnerable customers refer to page 19 of the Strategic report.

#### **Employees**

Employee roadshows are conducted annually and led by the Chief Executive to ensure that employees are kept informed about WPD's goals, objectives, performance, plans and importantly how individuals are able to contribute towards WPD's purpose and strategy. This year's roadshow consisted of 49 presentations, conducted across 33 locations.

Our internal communications through our in-house magazine and email updates are effective tools in engaging employees. In a recent internal publication, engagement from employees on RIIO-ED2 was invited, a demonstration that the directors are proactively seeking employees' views on key business areas.

An annual employee opinion satisfaction survey is conducted, with the results discussed at Board level. In response to the survey results, the Chief Executive published a workforce response action plan, which provides clear and transparent feedback to the staff on how the Board will respond to the survey.

Various presentations are delivered to employees to emphasise key priorities of the Group. For example, during the year, safety presentations were made to highlight and promote the importance the Board places on the safety of its workforce, contractors, customers and any member of the public coming into contact with the electricity network.

For the year ended 31 March 2020

#### Stakeholder relations and engagement (continued)

#### Employees (continued)

The Board acknowledges its responsibility towards its existing, as well as its retired, employees and thus WPD operates defined benefit pension schemes for its employees who joined the schemes prior to them being closed for new members, and defined contribution schemes for all other employees. A representative Board of trustees is established for the defined benefit pension schemes comprising representatives of the employer and plan participants. Assets held in trust are governed by UK regulations and practice and the schemes' investment strategy is decided by the Trustees in consultation with the employer. The Board is committed to the best interests of its employees, including past employees, and thus actively monitors the performance of its pension schemes. Relevant information is presented to the Board in board meetings.

For further details on engagement with employees please refer to page 4 and 17 of the Strategic report.

#### Regulators

The executive directors are actively involved in ensuring open and transparent communication with industry regulators, most notably Ofgem and the Health and Safety Executive ("HSE").

The directors engage Ofgem with the overall aim of developing a regulatory price control framework that contains the right balance of customer focused outputs and economic incentives, which help to deliver the Government's energy objectives and decarbonisation targets. All key communications and engagements with Ofgem are discussed at Board meetings.

The Chief Executive is a member of the National Health & Safety Committee ("HESAC"), (of which the HSE is a member), and either personally attends the committee meetings, or delegates a member of senior management to attend on his behalf. The goal is to align the WPD Group's internal safety campaigns to HSE safety initiatives and to HSE supported programmes.

The Chief Executive is a director of the industry trade association, the Energy Networks Association Limited ("ENA") and the chair of the ENA Electricity Network and Future Group.

Annually the Chief Executive or nominated members of the senior management team attend the UK's National Safety, Health and Environmental Committee for Energy.

#### Suppliers

Defined policies are in place for procurement of goods and services and associated supply chain management and engagement. We have a dedicated purchasing department that assists with engagement with suppliers. The Operations Director has oversight responsibility for logistics, including the supply chain function. Key issues are reported and discussed at the Executive Council.

We also carry out payment performance reporting for suppliers, details of which can be found on page 11 of the Strategic report.

#### **Shareholders**

The Board of Directors actively engages with our single shareholder, PPL, on all key matters. As stated above, the non-executive board members of WPD plc are part of PPL's senior management team. PPL's senior management has regular contact and dialogue with WPD's executive directors and senior management and all key information is fed back to the PPL Board on a timely basis. Regular financial and regulatory update meetings are conducted with PPL's management team to provide updates on any key accounting, business, and legal issues. Additionally WPD's financial plan is presented to PPL for detailed review and approval on an annual basis.

Further, for the benefit of all its current and future stakeholders, the Board is dedicated to conducting its business as a responsible steward of the environment. The Board actively monitors its impact in terms of carbon footprint, waste recycling and fluid loss. For details refer to pages 8, 9 and 16 of the Strategic report.

#### **Section 172 Statement**

For the year ended 31 March 2020

The directors of all UK companies must act in accordance with their duties under the Companies Act 2006. This includes a fundamental duty to promote the success of the Company for the benefit of its members as a whole. This duty has been central to the WPD Board's decision-making processes and outcomes over many years. The Board has well-established policies defining the Board's duties and responsibilities including those under Section 172.

The information below describes how, in performing their duties during the year, the directors have had regard to the matters set out in Section 172(1) (a) to (f) of the Act, and constitutes the Board's Section 172 Statement.

#### Strategy and long-term decision-making

Our strategy, as detailed on the page 2 of the Strategic report, clearly reflects that the Board is focused on promoting the success of the business by delivering customer focused performance in a manner that is environmentally sustainable, provides long term stability and meets the needs of its key stakeholders. Five key goals underpin our long term strategy: Safety, Network Performance & Security, Financial Stability, Environment and Stakeholder Value & Engagement. These goals form the basis of all of the Board's key decisions and the risk framework of the Group is linked to the achievement of these goals. The key goals are monitored by the Board through established key performance indicators ("KPIs"), as detailed in the Strategic report on pages 5 to 11.

The Board devolves day-to-day management and decision-making to its senior management team, and maintains oversight of the Company's performance, and reserves specific matters for approval. Policies are in place defining the powers of delegation by the Board, the matters reserved for the Board and the areas of responsibilities and accountability of each executive director. Policies have been established that define the framework within which we expect managers and employees to operate. These policies represent one of the means through which decisions on stakeholder interests are enacted.

By receiving regular updates on business programmes and objectives, the Board monitors that management is acting in accordance with agreed strategy. Processes are in place to ensure that the Board receives all relevant information to enable it to make well-judged decisions in support of the Company's long-term success. Refer to pages 22 and 23 in the Corporate governance statement for details on the integrity of information received by the Board.

The Board has oversight responsibility for the risk management framework of the Group and the Board ensures the alignment of strategy and the appetite for risk. For the purposes of business resilience, the Board satisfies itself that there is an appropriate risk management approach and that reasonable mitigations are in place for the key risks of the Group. For details on the Group's risk management approach refer to page 24 in the Corporate governance statement.

Refer to pages 28 to 30 for key decisions taken during the year.

#### **Employee interests**

Our business is built by our people and we are committed to ensuring that the employee interests are taken into consideration while promoting the success of the Group.

This is evident from the key decision taken during the year in relation to seeking a wider range of employee views through an expanded employee opinion survey. Refer to pages 29 and 30 of this statement for further details.

For additional details relating to employee engagement and key KPIs pertaining to our employees refer to pages 25-26 of our Corporate governance statement and pages 4, 10 and 17 of the Strategic report.

For details on our support for our employees during COVID-19 refer to page 11 of the Strategic report.

#### Stakeholder engagement

Our key stakeholders are customers, employees, regulators, suppliers and our shareholder. Our stakeholder engagement strategy is approved by the Executive Council annually. Detailed engagement with our stakeholders and regular reporting to them is conducted on our business plans, both reporting on our RIIO-ED1 commitments and developing our RIIO-ED2 priorities. Engagement on strategic areas and long term energy scenarios such as DSO, electric vehicle strategy etc. is also conducted. This demonstrates business planning built on stakeholder feedback.

Further details on engagement with each of our stakeholders is detailed on pages 25 to 26 of the Corporate governance statement. Further there are KPIs and action mitigating risks associated with each of these stakeholders that ensure that stakeholder relations are duly monitored by the Board. These can be found on pages 9 to 11 and 17 of the Strategic report.

#### **Section 172 Statement (continued)**

For the year ended 31 March 2020

#### Impact on communities and environment

The service we provide is critical to our communities and impacts the businesses and homes we serve on a daily basis. The directors believe that working closely with our communities is important in creating shared value for the business, the people we serve and the communities we operate in. During the year the directors directly, and indirectly through the senior management team, engaged with over 40,000 (2019: 35,000) stakeholders via a range of methods and delivered 300 (2019: 290) improvement actions based on feedback received. These actions cover a variety of stakeholder groups including the important areas of vulnerable customers and smart networks. We have supported over 18,000 (2019: 16,000) fuel poor customers in making £10m (2019: £6m) annual savings and proactively made contact with over 1 million customers during power cuts. Further details on our corporate social responsibility, including vulnerable customers, can be found on pages 18 to 20 of the Strategic report.

Looking to the future, we face exciting challenges as the UK works towards achieving the Government's de-carbonisation target of net-zero carbon emissions by 2050. We have long recognised the role that the electricity sector plays in contributing to the UK's ambitions towards carbon reduction. The directors remain focused on fostering an environment that supports innovation and creativity for ensuring that technology is utilised to best effect to meet the changing demands placed upon our network. The directors recognise our responsibility to operate in a way that minimises our impact on the environment, evident from the fact that environmental sustainability is one of our key goals. Details on this goal, related KPIs and mitigating actions for all key risks can be found on pages 3, 8, 9 and 16 of the Strategic report.

Further details are also available in our Environment & Innovation report available on our website at: <a href="https://www.westernpower.co.uk/customers-and-community/environment/carbon-impact-and-climate-change">https://www.westernpower.co.uk/customers-and-community/environment/carbon-impact-and-climate-change</a>

For details on our support for our communities during COVID-19 refer to pages 11 and 12 of the Strategic report.

#### Reputation for high standards and business conduct

The directors aspire to develop a culture where the management and workforce is motivated to be successful for its shareholder by creating long term value and at the same time is committed to satisfying customer needs. The directors also aim for us to be a valued member of the community, which includes acting as a responsible steward of the environment. The Board ensures that the strategy and goals of the Group support this. Our engagement with all stakeholder groups reflects that this aim is embedded across the business and impacts the decisions taken throughout the organisation.

Annual roadshows and senior leadership conferences are instrumental in driving a customer focused approach within each level of the organisation. Details of these engagements can be found on pages 21 and 25 of our Corporate governance statement.

Our vision and values are also communicated to each employee individually in their annual performance appraisals. A detailed vision statement is provided to each manager for this purpose which clearly outlines business priorities including the interests of our shareholder, our customers, the environment and the communities we serve, as key areas of focus for the Group. These areas are akin to the factors that need to be considered (as per section 172), in decision making throughout the organisation.

Annual training on "Standards of integrity", as endorsed by the Board, is mandatory for all employees including the executive directors. The main theme of this training is to reinforce to all staff the importance of acting with integrity and to conduct our business in accordance with our ethical standards. This training covers various topics such as dealing fairly with stakeholders, anti-bribery and anti-corruption considerations, conflicts of interest, the Modern Slavery Act 2015, the Equality Act 2010 and awareness of anti-bullying and harassment.

Further details on leadership by the Board can be found on page 21 of the Corporate governance statement.

Our commitment in this area is reflected in the fact that customers have rated us number one in stakeholder engagement incentive award (a key measure of Ofgem's broad measure of customer satisfaction) and we have an overall customer satisfaction score of 9.12 out of 10. We have continued to ensure customer satisfaction with our connections service, using customer feedback to develop our work plan for improving provision of connection services.

Our dedication to conducting our business with the highest standards of business conduct is also demonstrated by the emphasis placed by us on the safety environment within the organisation. Safety conferences and presentations are held each year to ensure that a safe working environment is a key priority throughout the organisation. There is a diligent system for reporting near misses and incidents to avoid future recurrences. Refer to our safety information on pages 3, 5 and 14 of the Strategic report.

#### Examples of key decisions during the year

We deliver an essential service and operate in a regulated environment. Key decisions are made within the parameters of the regulatory framework and the relevant price control period under which we are licensed to operate. The current RIIO-ED1 price control period commenced in April 2015 and runs through to March 2023. Examples of key decisions taken during the period to date include:

#### **Section 172 Statement (continued)**

For the year ended 31 March 2020

#### Examples of key decisions during the year (continued)

#### Developing a DSO Strategy

Transition from a Distribution Network Operator ("DNO") to a Distribution System Operator ("DSO") is an ongoing project that is likely to have a significant impact on the Group and its stakeholders in the future. The Board considers the shift from a DNO to a DSO essential to driving performance and efficiency from our network, enabling it to meet future energy demands of all our customers and contribute to the Government's target of net-zero carbon emissions by 2050. Our stakeholders will benefit as we transition to managing more active networks and we believe that informing and engaging our stakeholders on each step will help them to transition with us. The key stakeholders in relation to this transition are our customers, energy suppliers, technology providers/suppliers, local communities and regulators such as Ofgem, plus central Government via the Department of Business, Energy and Industrial Strategy ("BEIS").

In June 2017, we published our first DSO Strategy and Transition Plan, inviting key stakeholders including customer groups, industry and local enterprise partnerships, to review our proposals and provide feedback. At the end of this stage of the process, a DSO strategy launch event was conducted, where we presented our DSO strategy to more than 120 attendees consisting of a wide range of stakeholders. These attendees were given an opportunity to pose questions to a panel of industry experts. In addition to that, we also hosted a series of DSO round table sessions, allowing various stakeholders to shape our future as we transition to being a DSO. These were carried out across all four licence areas and engaged a broad cross section of customer representatives and allowed WPD to further refine some of the initial messaging received during consultation. Following these engagements a formal consultation document was published which highlighted the actions to be taken by WPD in response to the key feedback items and the DSO strategy was updated to reflect the feedback. In the current year, to keep our customers and other stakeholders updated at all times, we have published a revised DSO plan, and will continue to update it as thinking evolves.

This process, through which our DSO strategy has been developed, and is supported by a published DSO plan, highlights the commitment of the directors to promote the interests of the Group in a manner that is aligned with the needs and priorities of our stakeholders. We aim to develop a successful DSO strategy by taking into account the needs and views of our stakeholder groups as well as considering the long term impact of our decisions. This is further demonstrated as below:

- Details on how WPD factored in customer views on key principles of DSO strategy could be found on pages 10, 11, 12, 17 and 19 in the DSO strategy document published on our website at the link below:
   https://www.westernpower.co.uk/smarter-networks/network-strategy/dso-strategy
- Engagement and consideration of feedback from regulators has also been a prime factor of consideration for the directors. In the current year, one such example is WPD's decision to separate DSO activities into a separate management structure. This was done in response to BEIS and Ofgem requiring the DNOs to address the potential conflicts of interest between asset solutions and use of third party flexibility. Concerns over this conflict had been raised by suppliers, aggregators and parts of the Distributed Generation community.
- The directors are actively engaged in developing the industry transition towards DSO, through leading on the ENA's Open Networks Project that aims to coordinate the DSO transition at industry level by designing, testing and implementing the whole system elements which will bring benefits to all energy system participants. This project demonstrates the directors' commitment to contribute to and play an active role for the industry as a whole.
- The directors are also committed to working proactively with community energy groups and recognise that the volunteer led approach and complex nature of their projects means that community energy groups need more time and support to engage in the process of connecting to the network. We run eight Community Energy Events every year at key locations where community energy groups can come to find out what is happening in the industry. Our Multi Asset Demand Execution ("MADE") demonstrates our commitment to understanding the impact of future low carbon technologies onto community energy. We will, throughout the transition, ensure that communities will be an integral part of the transition to a smarter and more flexible system.

#### Staff engagement

In the current year, we refreshed and revised the format of the employee opinion survey. This was an initiative led by the Chief Executive. The survey was made online for the first time and opinion was sought on a broader range of areas than ever previously undertaken. The number of questions in the survey increased to 53 from 12 in previous years.

This decision was taken so as to enable the Board, and the owners, to get a much clearer picture of the views of staff by covering categories such as safety, wellbeing, ethics, diversity and inclusion, performance management, recognition and reward, effectiveness of communication and effectiveness of collaboration.

#### **Section 172 Statement (continued)**

For the year ended 31 March 2020

#### Examples of key decisions during the year (continued)

#### Staff engagement

The results of the survey were discussed at the leadership conference with 90 senior managers and based on the feedback an 'action plan' has been developed.

The key strengths identified by the survey were very encouraging and the directors have taken note of these and are committed to building upon them. These were identified as:

- Our workforce recognise, as they have for a long time, the necessity of safety precautions that are undertaken whilst completing work:
- We are committed to exceeding customer expectations;
- We have strong staff commitment that is evident from the high proportion of staff intending to stay working for WPD for at least the next year;
- We deliver work of a high quality and this is recognised as a clear team commitment; and
- Our workforce has excellent awareness across the whole business of the WPD mission and values.

More importantly, the survey highlighted the key areas of opportunity where the directors will focus and are committed to make positive change:

- We will focus on increasing the transparency and equality of the potential for individual growth and development opportunities across the whole business;
- We will demonstrate that the feedback from the employee survey will be used for making improvements;
- We will encourage the whole workforce to share ideas about opportunities the business could take advantage of;
- We will support and increase the transparency of opportunities for professional growth of all employees; and
- We will develop more effective co-operation across the different functional areas of the business.

The directors have committed to sharing the actions taken and ensuring that the progress of those actions are communicated to the whole workforce.

This initiative highlights the commitment of the directors to ensure that employee interests are taken into consideration while promoting the success of the Group. Development of an action plan based on the survey results demonstrates that the Board is committed to making improvements based on feedback from staff and to developing an environment of open communication and enhancing employee engagement.

#### **Declaration** of dividend

During the year the Board has declared a dividend of £200.1m (2019: £300.2m). In considering capital distributions, the Board is mindful of stakeholders' views and takes account of our latest financial position, the long-term sustainability for the WPD Group in addition to the allowed rate of return and any incentive rewards received. In its capacity of providing oversight for the operational performance of the business, the Board also takes account of the prevailing performance against customer performance targets, other RIIO-ED1 output commitments and future requirements such as DSO, to assess whether there are any additional investment needs.

As part of the regulatory process, Ofgem sets the allowed rate of return within each price control period; for RIIO-ED1 this is set at 6.4%. As is evident from the levels of our annual capital expenditure (see page 7 of the Strategic report), we reinvest a significant portion of our profits back into the network to ensure an efficient, reliable and environmentally sustainable network. The Board ensures that it understands and takes account of the views of our shareholder in order to preserve positive investor relations and maintain secure and continuous investment. The Board acts in the shareholder's best interests by proposing an amount of dividend in accordance with the financial parameters of our regulatory allowance whilst maintaining strong financial health metrics.

#### Directors' report

For the year ended 31 March 2020

The directors present their annual report on the affairs of the WPD group, together with financial statements and auditor's report, for the year ended 31 March 2020.

#### Results and dividends

The WPD Group reports a profit for the financial year of £548.6m (2019: £604.5m). Profit before tax is £749.7m (2019: £733.2m).

The WPD Group also reports other comprehensive gains, which were posted directly to capital and reserves, of £224.6m (2019: £104.7m). This primarily relates to the defined benefit pension plan remeasurement, net of tax.

Dividends of £200.1m have been paid during the year (2019: £300.2m).

All dividend payments are made out of the distributable reserves of the Company.

#### Political affiliations, donations and expenditure

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

WPD does not engage in any lobbying activities with the Government. As part of the RIIO-ED2 price control process, WPD engages with a wide range of stakeholders to seek their input on the business plan which then drives the outputs that the Group delivers. WPD is also a member of various trade associations, such as the Energy Network Association ("ENA"), that provide a strategic focus and channel of communication for the industry.

#### Financial assistance from the Government

WPD has not received any financial assistance from the Government during the year. The Group can potentially access an additional 10% of its Apprenticeship Levy payments in order to fund approved training programmes for apprentices; however, for the year ended 31 March 2020, the payments into the fund by the Group were in excess of the funding the Group reclaimed.

#### Financial risk management objectives and policies

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

For further details of risks in relation to treasury operations, see the "Risk management and controls" section of the Strategic report.

#### Liquidity and going concern

The following credit facilities were in place at 31 March 2020, in respect of which all conditions present had been met at that date.

	Expiration date	Capacity £m	Borrowed £m	Letters of credit issued £m	Capacity £m
WPD plc - Syndicated Credit Facility	Jan. 2023	210.0	161.0	-	49.0
WPD South West - Syndicated Credit Facility	<b>July 2021</b>	245.0	100.0	-	145.0
WPD East Midlands - Syndicated Credit Facility	<b>July 2021</b>	300.0	-	-	300.0
WPD West Midlands - Syndicated Credit Facility	<b>July 2021</b>	300.0	-	-	300.0
Uncommitted Credit Facilities		100.0	-	3.5	96.5
Total Credit Facilities		1,155.0	261.0	3.5	890.5

WPD plc also has a loan facility agreement dated April 2015 from PPL Capital Funding, Inc, an entity within the PPL Corporation group, for \$125m. This facility expires in December 2028 and has never been drawn against.

The Group intends to issue debt over the next 12 months and forward starting interest rate swaps have been issued to minimise the exposure to any cash flow interest rate risk.

As at 31 March 2020 and 31 March 2019 the WPD Group had the following debt:

	External debt outstanding				Cash and short term	
	Long-term		Short-term		deposits	
	2020	2019	2020	2019	2020	2019
	£m	£m	£m	£m	£m	£m
WPD South West	1,020.00	1,010.90	113.6	19.5	41.9	62.2
WPD South Wales	507.6	659.3	151.6	-	0.5	4.6
WPD East Midlands	1,658.3	1,404.5	-	90.5	108.6	2.5
WPD West Midlands	1,473.7	1,472.2	-	-	5.6	12.8
Western Power Distribution plc	1,451.4	1,372.6	161.0	153.4	10.3	28.4
Other subsidiaries	-	-	-	-	34.1	32.2
	6,111.0	5,919.5	426.2	263.4	201.0	142.7

#### Directors' report (continued)

For the year ended 31 March 2020

#### Financial risk management objectives and policies (continued)

Liquidity and going concern (continued)

Short-term debt includes bank overdrafts of £13.5m (2019: £19.5m). Short term deposits are considered corporate assets and can be accessed by any entity within the Group. In addition to the cash and short term deposits above, the WPD Group's parent, Western Power Distribution plc, had made a loan to its parent of £161.9m (2019: £154.9m) which is maturing in 2021.

The Group has net current liabilities of £490.5m (2019: £420.6m). The Group's net current liabilities will be settled with a combination of cash flows from operating activities, use of existing facilities, and issuances of long-term debt.

The directors have considered the availability of facilities as set out above, the relatively stable and regulated nature of the business, the forecast long term business plan, the credit ratings of WPD and the anticipated ability of the WPD Group to be able to raise additional long term debt in the future.

The directors have assessed the principal risks discussed in the Strategic report (pages 14 to 18) and the impacts of COVID-19 and related uncertainties have also been taken into consideration in arriving at the going concern assumption for the preparation of the financial statements.

DNOs are essential in keeping critical infrastructure assets operating safely and securely and in making sure that homes and businesses across the country are receiving the energy needed. The work of WPD is an essential part of the country's response to COVID-19, as what we do is crucial for the continuation of existing essential services, the establishment of new critical infrastructures and for keeping the public, including the most vulnerable in our society, safe. Therefore, even in these unprecedented times, where many business sectors are impacted severely, WPD has a continuing licence obligation to be a sustainable business and to continue to provide essential services to our customers.

Allowed revenues are fixed over a price control period and any adverse impact on revenues due to COVID-19 is considered a temporary cash flow implication and is expected to be recovered in future years. Some of the material cash flow impacts that have been taken into consideration are:

- Reduction in demand leading to reduced DUoS revenues;
- Working capital implications as a result of changes to operational work programmes;
- Reduction in cash outflow associated with capital work due to Government restrictions;
- Reduction in customer driven non-trade recharge activities and associated revenue;
- Ofgem's supplier payment deferral scheme.

After consideration of all cash flow impacts related to the pandemic, the Group has sufficient liquidity over the next 12 months. A reasonable worst case scenario plan, considering an extension of Government restrictions until the end of 2020, has been deliberated by the Group; under this scenario there is sufficient headroom available in order to meet liquidity and covenant requirements.

WPD is actively monitoring the recovery of trade receivables and our overall liquidity position. Since March 2020 to date there has been no material slowdown in the cash receipts of the Group.

The Group has £456m of debt due for repayment within the next 12 months from the date of signing of the accounts. The Group intends to raise long term debt within the next 12 months. However, if market conditions are not favourable, the Group has sufficient head room available under existing committed facilities to meet all cash flow needs.

In May 2020, the syndicated credit facility detailed above, expiring in July 2021, was terminated early. This was replaced with a combined facility of £845.0m expiring in May 2023. The facility is shared across the four DNOs as follows:

South West £220.0m South Wales £125.0m East Midlands £250.0m West Midlands £250.0m

Due to the licensed regulatory obligations of the business, the necessity of continued operations during this time of economic crisis and having access to sufficient liquidity, under a variety scenarios, the Group does not consider that there is material uncertainty over the entity's ability to continue as a going concern.

Thus, the directors have concluded that the WPD Group has sufficient resources available to enable it to continue in existence for the foreseeable future and for a period of at least 12 months from the date of signing the accounts and have therefore continued to adopt the going concern basis in preparing the financial statements.

#### Group debt

The WPD Group is structured such that a proportion of the WPD Group's debt is issued by the holding company Western Power Distribution plc. Interest payments on this debt, together with other items, are funded primarily through dividend payments from WPD South West, WPD South Wales, WPD East Midlands and WPD West Midlands.

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

For the year ended 31 March 2020

#### **Corporate governance statement**

The Group's Corporate governance statement is detailed on pages 21 to 26.

#### **Employee engagement statement**

Details of the directors' engagement during the year with employees and consideration of employees' interests can be found in the Corporate governance statement on pages 21, 25 and 26.

The key decision on staff engagement, as detailed in our Section 172 statement, illustrates how employees' interests are always taken into account. For more details see pages 29 and 30.

#### **Business relationships statement**

The Group's key business relations are with its customers, suppliers and regulators. Details of how the directors foster the Group's business relationships and have regard to their interests have been stated in our Strategic report, Corporate governance statement and Section 172 statement.

#### Customers

- Strategic report see pages 3, 4, 9, 10 and 17;
- Corporate governance statement see page 25;
- Section 172 statement the key decision in relation to our DSO strategy outlines how customer interests have been considered at each step of transitioning to DSO. See page 29.

#### Suppliers

- Strategic report see page 4 and 11;
- Corporate governance statement see page 26.

#### Regulators

- Strategic report see page 4 and 17;
- Corporate governance statement see page 26.

#### Strategic report

The following information required in the Directors' report has been included in the Strategic report:

- an indication of future developments in the business see page 12 and 13;
- an indication of activities of the Company in the field of research and development see page 13;
- a statement on the policy for disabled employees see page 4;
- employee policies see page 4.

#### Streamline energy and carbon reporting ('SECR') $\,$

Total annual quantity of emissions using equivalent tonnes of carbon dioxide ("tCO2e") - including own use

	tCO <sub>2</sub> e		tCO2e per employee	
	2020	2019	2020	2019
Scope 1 (direct emissions)				
Operational transport	37,621	32,215	5.72	4.85
SF6 gas	9,005	10,934	1.37	1.65
Fuel combustion (diesel / gas oil)	9,249	9,218	1.41	1.39
Buildings	211	246	0.03	0.04
	56,086	52,613	8.53	7.93
Scope 2 (energy indirect emissions)				
Buildings electricity	5,289	5,877	0.80	0.88
Substation electricity	12,129	17,260	1.84	2.60
WPD Telecoms	804	577	0.12	0.09
	18,222	23,714	2.76	3.57
Total scope 1 & 2	74,308	76,327	11.29	11.50
Scope 3 (other indirect emissions)				
Business transport	3,606	3,437	0.55	0.52
Total scope 1, 2 & 3	77,914	79,764	11.84	12.02

The Group's chosen intensity measurement is tonnes of carbon dioxide equivalent per employee.

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

For the year ended 31 March 2020

#### Streamline energy and carbon reporting ('SECR') (continued)

Aggregate in kWH of annual quantity of energy consumed for business activities and own use Electricity energy consumed for the year to 31 March 2020 is kWH 23,259,982 (2019: kWH 22,800,569).

Gas energy consumed for the year to 31 March 2020 is kWH 1,150,183 (2019: kWH 1,149,182).

Energy consumed for helicopters for the year to 31 March 2020 is kWH 4,478,197 (2019: kWH 6,700,983).

Methodologies used in calculating energy and carbon reporting data

Our BCF details the impact that our operational activities have on the environment in terms of tCO2e emissions and takes account of our energy usage from offices, transport emissions (operational and business), fuel combustion and the release of greenhouse gases (SF6). The reported data for operational transport (road) and fuel combustion also takes account of a number of our larger contractor emissions as required under the Ofgem reporting requirements.

The data compiled and reported by the Group follows a recognised methodology as described within international business carbon footprint standards, the Greenhouse Gas ("GHG") reporting protocol and ISO14064-1. ISO14064-1 specifies principles and requirements at the organisation level for quantification and reporting of GHG emissions and removals. Our published BCF data has been verified and data assured for accuracy and compliance with the standards detailed above.

Measures for increasing the Group's efficiency during the year

During 2019/20, the Group has implemented the following energy efficiency measures:

- replacement of older operational fleet vehicles with more fuel efficient alternatives and improving awareness of the impacts of driving style on fuel efficiency and vehicle emissions;
- continuing to trial and purchase electric operational fleet vehicles;
- installation of electric vehicle charging points at many of our non-operational depot sites for both fleet and employee owned electric vehicles;
- improvements to the reporting of SF6 gas leaks from our installed equipment and fully utilising the infrared SF6 detection cameras enabling us to quickly pinpoint the source of leaks;
- ensuring that all newly built WPD depots achieve the UK Building Research Establishment Environment Assessment Method ("BREEAM") standard of 'Excellent' as a minimum and that refurbished existing depots achieve the 'Very Good' standard;
- the on-going replacement with more modern and energy efficient heating and cooling systems throughout our property portfolio plus undertaking an energy efficiency review at many of our non-operational and operational sites including employee energy awareness campaigns.

#### Subsequent events

Subsequent to the year-end, on 15 June 2020, the Company paid an interim dividend of £30.0m to PPL WPD Investments Limited.

Subsequent to the year-end, on 7 April 2020, the share capital of the Company was reduced by £600m. The share capital reduction was approved by the directors on 28 February 2020.

#### Directors and their interests

The directors who served during the year and subsequently were as follows:

P Swift, Chief Executive
GR Halladay, Operations Director
IR Williams, Finance Director
AJ Sleightholm, Resources and External Affairs Director
V Sorgi
AJ Torok
GN Dudkin
JH Raphael
JP Bergstein Jr (appointed 1 July 2019)

# **Directors' report (continued)**

For the year ended 31 March 2020

# **Directors and their interests (continued)**

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

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

#### Statement of disclosure to independent auditor

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, of which the auditor is unaware. Each 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 auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

#### **Independent auditor**

Deloitte LLP have expressed their willingness to continue in office and a resolution proposing their reappointment will be put before the Annual General Meeting.

Registered Number: 9223384

Approved by the Board and signed on its behalf by:

P Swift

Chief Executive

Pilish

23 July 2020

**Western Power Distribution plc** 

Avonbank Feeder Road Bristol BS2 0TB

#### Directors' responsibilities statement

The directors are responsible for preparing the Annual Report and Financial Statements, including the WPD Group financial statements and the Company financial statements, the Strategic report and the Directors' report in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the WPD Group financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union and the parent company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom accounting standards and applicable law), including Financial Reporting Standard ("FRS") 101 "Reduced Disclosure Framework".

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 Group and the parent Company and of the profit or loss of the Group for that period.

In preparing the Group financial statements, the directors are required to:

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

In preparing the Company financial statements, the directors are required to:

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company on a consolidated and individual basis, and to enable them to ensure that the individual and consolidated financial statements comply with the Companies Act 2006 and, with regard to the Group financial statements, article 4 of the IAS regulation. They are also responsible for the system of internal control, for safeguarding the assets of the Company and its subsidiaries and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Information published on the Company's website is accessible in many countries with different legal requirements. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

# Report on the audit of the financial statements

#### 1. Opinion

In our opinion:

- the financial statements of Western Power Distribution Plc (the 'parent Company') and its subsidiaries (the 'Group') give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 March 2020 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union;
- the parent Company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements which comprise:

- the consolidated income statement:
- the consolidated statement of comprehensive income;
- the consolidated and parent Company statement of changes in equity;
- the consolidated and parent Company balance sheet;
- the consolidated cash flow statement;
- the related notes 1 to 34.

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent Company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

#### 2. Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Group and the parent Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's ("the FRC's") Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. The non-audit services provided to the Group and the parent Company for the year are disclosed in note 5 to the financial statements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the parent Company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### 3. Summary of our audit approach

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Key audit matters	The key audit matters that we identified in the current year were:						
	• Impairment of goodwill;						
	Capitalisation of overheads; and						
	Pension asset valuation.						
	Within this report, key audit matters are identified as follows:						
	Newly identified						
	Increased level of risk						
	Similar level of risk						
	Decreased level of risk						
Materiality	The materiality that we used for the Group financial statements was £37.5m (2019: £36.7m) which was						
	determined on the basis of 5% (2019: 5%) of profit before tax.						
Scoping	Based on our assessment, we focused our Group audit work on four components which were subject to						
	a full scope audit of their financial information. Our full scope audit covered substantially all of the						
	Group's revenue, profit before tax and net assets.						

# 3. Summary of our audit approach (continued)

# Significant changes in our approach

As a consequence of the Covid-19 outbreak, there has been an increased level of risk and volatility as at the year-end of certain markets to which the Group is exposed. This includes property markets where the Group's pension scheme assets are partially invested. As a result we have considered the valuation of pension assets as a new key audit matter due to external valuers including material uncertainty clauses in property asset valuations as at 31 March 2020 in response to the market volatility and

In the current year, we have identified a fraud risk in relation to the goodwill impairment model. This is due to there being several changes made to assumptions within the impairment model, particularly the RIIO-ED2 cash flows and terminal RAV multiple, combined with the limited headroom in the base case

There have been no other significant changes to our audit approach.

#### 4. Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Group's or the parent Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

#### 5. Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included 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.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

5.1. Impairment of goodwill



# Key audit matter description

Management is required to assess the carrying value of goodwill and acquired intangibles, and perform an impairment review under IAS 36 Impairment of Assets on an annual basis and whenever an indication of impairment exists. Goodwill was acquired through business combinations.

As disclosed in note 15 of the financial statements the carrying value of goodwill in relation to East Midlands is £518.8m (2019: £518.8m), West Midlands £614.4m (2019: £614.4m) and South Wales £120.9m (2019: £120.9m).

We have identified a key audit matter around key assumptions used in management's impairment model. The most complex assumptions that require a significant amount of judgement are the overall returns on forecast cash flows over the RIIO ED2 price control period, the discount rate used to calculate the present value of future cash flows and the premium applied to the Regulatory Asset Value ("RAV") at the end of the cash flow period for each cash generating unit.

In the current year, we have identified a fraud risk in relation to the goodwill impairment model. This is due to there being several changes made to assumptions within the impairment model, particularly the RIIO-ED2 cash flows and terminal RAV multiple, combined with the limited headroom in the base case calculation. As a result, we have concluded that the risk relating to this key audit matter has increased since the prior year.

Refer to note 1 'significant accounting policies', note 2 'critical accounting judgements and key sources of estimation uncertainty' and note 15 'intangible assets' in the financial statements for further discussion of the Group's policy and judgements in the goodwill impairment review.

#### Independent auditor's report

to the members of Western Power Distribution plc (continued)

#### 5. Key audit matters (continued)

#### 5.1. Impairment of goodwill (continued)

# How the scope of our audit responded to the key audit matter

We have performed the following procedures around this key audit matter:

- Obtained an understanding of and testing relevant key controls around determining the key inputs being the forecast RIIO ED2 cash flows, the discount rate and the premium applied to the RAV at the end of the cash flow period.
- · Challenged underlying cash flow forecasts, with reference to Ofgem guidance on RIIO ED2 returns on regulated equity and incentive revenues.
- Worked with our internal valuation specialists to challenge the reasonableness of the discount rate and premium applied to the RAV at the end of the cash flow period.
- Challenged management's position using key assumptions developed independently based on external market data.
- Reviewed and recalculated management's sensitivity analysis on the key assumptions.
- Developed independent expectations of goodwill impairment through the use of more prudent assumptions around returns in the RIIO ED2 cash flow period.
- Assessed the adequacy of the Group's disclosures of the sensitivity and reasonably possible changes of the East Midlands, West Midlands and South Wales cash generating units to changes in the key assumptions.

We conclude that key assumptions underpinning the value in use calculation used by the Group in its assessment of the carrying value of goodwill for each of the three CGUs, when considered in aggregate, lie at the optimistic end of the range of reasonable estimates that we judge appropriate.

We concur with management's view that no impairment charge is required for the current year.

*5.2. Capitalisation of overheads* 



#### Key audit matter description

Amounts capitalised as network assets include indirect costs associated with corporate overhead costs. The costs are capitalised based on management's assessment of the costs incurred that are directly attributable to the capital work performed.

A key audit matter has been identified in respect of the key assumptions relating to the capitalisation of corporate overheads.

There is a judgement in relation to the nature of costs included within each cost classification; and a management estimate in relation to the appropriate percentage of costs to capitalise.

Due to the estimation required in assessing the value to be capitalised, we have determined that there was a potential for fraud through possible manipulation of capitalisation rates.

Total corporate overheads are £122.3m in the year (2019: £119.5m), of which £73.5m (2019: £73.4m) has been capitalised to fixed

Refer to note 1 'significant accounting policies', note 2 'critical accounting judgements and key sources of estimation uncertainty' and note 12 'property plant and equipment' in the financial statements for further discussion of the Group's policy and judgements in capitalisation of overheads.

# How the scope of our audit responded to the key audit matter

We have performed the following procedures around this key audit matter:

- Obtained an understanding and tested the relevant key controls related to the estimate of corporate overhead costs, and those that are directly associated with capital projects and capitalisation rates.
- Evaluated the appropriateness of the accounting treatment for capitalising overheads by reference to the requirements of IAS 16 Property, Plant and Equipment.
- Reviewed the policies, procedures and assumptions used in estimating the value of overheads that are directly attributable to capital projects.

#### Independent auditor's report

to the members of Western Power Distribution plc (continued)

#### 5. Key audit matters (continued)

#### 5.2. Capitalisation of overheads (continued)

#### How the scope of our audit responded to the key audit matter (continued)

- Agreed a sample of costs capitalised to appropriate audit evidence to test that they have been recorded accurately.
- Tested mangagement's estimate of percentage of costs that are directly attributable to capital projects through verifying the inputs into the calculation and agreeing these to appropriate support and evidence.
- Challenged management's methodology and estimate through considering whether there are alternative appropriate assumptions.

#### Key observations

Based on the work performed we are satisfied that the assumptions made in respect of the capitalisation rates applied to corporate overheads within the fixed assets balance are reasonable as at 31 March 2020.

#### 5.3. Pension asset valuation



#### Key audit matter description

The retirement benefit obligation of the Group includes assets totalling £6,635.5m (£6,646.2m) of which £402.3m (2019: 379.9m), 6.1% (2019: 5.7%), are property assets.

Consistent with guidance provided by the Royal Institute of Chartered Surveyors ("RICS"), the external valuers' reports, include "material valuation uncertainty" in respect of pension property assets due to the Covid-19 pandemic leading to increased risk and volatility in property valuations as at 31 March 2020.

Given the estimation uncertainty could give rise to a range of valuations, we identified a key audit matter associated with the valuation of property assets within the pension asset portfolio.

Refer to note 1 'significant accounting policies', note 2 'critical accounting judgements and key sources of estimation uncertainty', and note 27 'retirement benefit obligations' in the financial statements for further discussion of the Group's policy and valuation judgements in pension property assets.

# How the scope of our audit responded to the key audit matter

We have performed the following procedures around this key audit matter:

- Obtained an understanding of and tested the relevant key controls over the valuation of pension property assets.
- Obtained details of the property funds that include material uncertainties from the investment managers and reviewed a summary of the pension property assets in the funds to understand their nature.
- Challenged management's valuation, with input from our internal valuation specialists, of certain pension property assets. Our work included verifying that the valuation methodologies are in accordance with RICS guidance and suitable for use in determining the carrying value in the balance sheet.
- Developed an independent valuation through reviewing publically available information on these assets and other independent sources, and comparing it to the inputs used by management to determine the asset values.

#### Key observations

We consider management's valuation of pension property assets to be reasonable and the disclosures in the financial statements regarding the estimation uncertainty and sensitivity of the pension assets are appropriate at 31 March 2020.

# 6. Our application of materiality

#### 6.1 Materiality

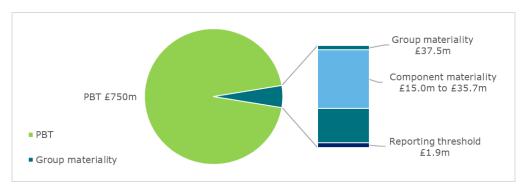
We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

# 6. Our application of materiality (continued)

#### 6.1 Materiality (continued)

	Group financial statements	Parent Company financial statements
Materiality	£37.5m (2019: £36.7m)	£15.1m (2019: £14.7m)
	5% of profit before tax. This is consistent	Parent Company equates to less than 1% of
	with the methodology applied in 2019.	net assets. The materiality is capped at
Basis for determining materiality		40% of Group materiality. This is
		consistent with the methodology applied in
		2019.
	We have determined materiality based on	We have determined materiality based on
	profit before tax as this is the key metric	net assets as the Company holds the
Rationale for the benchmark applied	used by management, investors, analysts	investments for its subsidiary companies.
	and lenders, with shareholder value being	Therefore a balance sheet basis is to be
	driven by the result.	appropriate.



#### 6.2 Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. Group performance materiality was set at 70% (2019: 70%) of Group materiality for the 2020 audit. In determining performance materiality, we considered the following

- Our cumulative experience from prior year audits;
- The low level of corrected and uncorrected misstatements identified;
- Our risk assessment, including our understanding of the entity and its environment; and
- Our assessment of the Group's overall control environment and that we consider it appropriate to rely on internal controls over property, plant and equipment; revenue; operating expenses and payroll.

# 6.3. Error reporting threshold

We agreed with the Board of Directors that we would report to the Board all audit differences in excess of £1.9m (2019: £1.7m), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Board of Directors on disclosure matters that we identified when assessing the overall presentation of the financial statements.

# 7. An overview of the scope of our audit

#### 7.1. Identification and scoping of components

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material misstatement at the Group level. Based on that assessment we focused our group audit scope primarily on the audit work at four components, which were subject to a full scope audit. Analytical procedures were performed on the remaining non-significant components. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

Those four components represent the principal business unit within the Group and account for over 98% (2019: 99%) of revenue, profit before tax and net assets. They were also selected to provide an appropriate basis for undertaking audit work to address the risks of material misstatement identified above. Our audit work of the four components was executed at a level of materiality applicable to the individual component and was lower than Group materiality. Component materiality ranged from £15.0m-£35.7m (2019: £14.6m-£34.8m).

The parent Company is located in Bristol and audited directly by the group audit engagement team.

# Independent auditor's report to the members of Western Power Distribution plc (continued)

# 7. An overview of the scope of our audit (continued)

#### 7.2. Our consideration of the control environment

The Group's IT landscape contains a number of IT systems, applications and tools used to support business processes and for reporting. In line with our scoping of components (see section 7.1) our work in relation to IT controls focuses on the four identified components. We performed an independent risk assessment of the systems, applications and tools to determine those which are of greatest relevance to the Group's financial reporting, including those that contain system configured automated controls that host financially relevant data and associated reports.

Using our specialists, we performed testing of General IT controls of these systems, typically covering controls surrounding user access management, change management and interfaces with other systems relating to in scope IT systems as well as controls over key reports generated from the IT systems and their supporting infrastructure.

In order to evaluate the operating effectiveness of IT controls, we performed walkthrough procedures of the key controls relevant to the business cycles, including property, plant and equipment; revenue; operating expenses and payroll to understand whether the controls were effectively designed to address the IT related risk. We subsequently performed testing of the controls across the audit period, to determine whether the controls had been consistently applied as designed.

Our procedures enabled us to place reliance on IT controls, as planned, in the audit approach across a number of business cycles (see section 6.2).

#### 8. Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

# We have nothing to report in respect of these matters.

# 9. Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group's and the parent 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 the directors either intend to liquidate the Group or Company or to cease operations, or have no realistic alternative but to do so.

# 10. Auditor's responsibilities for the audit of the financial statements

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 error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud and non-compliance with laws and regulations are set out below.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

#### Independent auditor's report

#### to the members of Western Power Distribution plc (continued)

#### 11. Extent to which the audit was considered capable of detecting irregularities, including fraud

We identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and then design and perform audit procedures responsive to those risks, including obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion.

#### 11.1. Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we consider the following:

- the nature of the industry and sector, control environment and business performance including the design of the Group's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management, internal audit, and the Board of Directors about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Group's documentation of their policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance:
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;
- the matters discussed among the audit engagement team and involving relevant internal specialists, including tax, valuations, pensions, IT and real estate specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the impairment of goodwill and inappropriate capitalisation of corporate overheads. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the Group operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the financial statements. The key laws and regulations we considered in this context included the UK Companies Act, Listing Rules, pensions legislation and tax legislation.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the Group's ability to operate or to avoid a material penalty. These included the Group's operating licence as set out by the energy regulator, Ofgem, which is fundamental to the Group's ability to continue as a going concern.

# 11.2. Audit response to risks identified

As a result of performing the above, we identified the impairment of goodwill and capitalisation of corporate overheads as key audit matters related to the potential risk of fraud. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters.

In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- enquiring of management, the Board of Directors, and external legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with relevant regulators including HMRC and Ofgem; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

# Independent auditor's report to the members of Western Power Distribution plc (continued)

# Report on other legal and regulatory requirements

#### 12. Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic report and the Directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Group, the parent Company and their environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic report or the Directors' report.

#### 13. Matters on which we are required to report by exception

#### 13.1. Adequacy of explanations received and accounting records

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company financial statements are not in agreement with the accounting records and returns.

# We have nothing to report in respect of these matters.

#### 13.2. Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made.

We have nothing to report in respect of these matters.

#### 14. Other matters

#### 14.1 Auditor tenure

Following the recommendation of the Board of Directors, we were appointed by the shareholders on 16 June 2017 to audit the financial statements for the year ending 31 March 2017 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is four years, covering the years ending 31 March 2017 to 31 March 2020.

# 14.2 Consistency of the audit report with the additional report to the Board of Directors

Our audit opinion is consistent with the additional report to the Board of Directors we are required to provide in accordance with ISAs (UK).

# 15. Use of our report

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.

Dewith Jones

Delyth Jones (Senior statutory auditor) For and on behalf of Deloitte LLP Statutory Auditor Bristol, United Kingdom 28 July 2020

# Western Power Distribution plc consolidated income statement

For the year ended 31 March 2020

	Note	2020 £m	2019 £m
Revenue	3	1,723.5	1,685.6
Operating costs	5	(684.8)	(680.9)
Other operating income	6	0.5	6.2
Other operating expense	6	(2.0)	(1.0)
Operating profit	3	1,037.2	1,009.9
Finance income	7	11.5	10.2
Finance costs	7	(301.0)	(282.6)
Net finance income/(expense) relating to pensions and			
other post-retirement benefits	27	2.0	(4.3)
Profit before income tax		749.7	733.2
Income tax expense	10	(201.1)	(128.7)
Profit for the year attributable to equity holders of the parent		548.6	604.5

All operations are continuing.

The accompanying notes 1 to 34 are an integral part of these financial statements.

# Western Power Distribution plc consolidated statement of comprehensive income

For the year ended 31 March 2020

	Note	2020 £m	2019 £m
	Note	žiii	ĮIII –
Profit for the year		548.6	604.5
Other comprehensive income:			
Other comprehensive income/(expense) to be reclassified to profit o	r loss in subsequent per	riods:	
Profit arising on cash flow hedges during the year		40.4	59.4
Reclassification adjustments for losses on cash flow hedges			
included in profit or loss (finance costs)		(32.6)	(44.2)
Income tax effect	10	(1.4)	(2.5)
		6.4	12.7
Other comprehensive income not to be reclassified to profit or loss to	in subsequent periods:		
Re-measurement gains on defined benefit pension plan	27	284.9	117.4
Income tax effect	10	(66.7)	(25.4)
		218.2	92.0
Other comprehensive income for the year, net of tax		224.6	104.7
Total comprehensive income for the year, net of tax, attributable to equity holders of the parent		773.2	709.2

# Western Power Distribution plc consolidated statement of changes in equity

For the year ended 31 March 2020

	Note	Share capital £m	Merger reserve £m	Hedging reserve £m	Retained earnings £m	Total equity £m
At 1 April 2018		1,657.6	(963.1)	(17.9)	3,627.1	4,303.7
Profit for the year Other comprehensive income		-	-	12.7	604.5 92.0	604.5 104.7
Total comprehensive income for the year		-	-	12.7	696.5	709.2
Equity dividends paid	11	-	-	-	(300.2)	(300.2)
At 31 March 2019		1,657.6	(963.1)	(5.2)	4,023.4	4,712.7
Profit for the year Other comprehensive income		-	-	6.4	548.6 218.2	548.6 224.6
Total comprehensive income for the year		-	-	6.4	766.8	773.2
Equity dividends paid	11	-	-	-	(200.1)	(200.1)
At 31 March 2020		1,657.6	(963.1)	1.2	4,590.1	5,285.8

# Western Power Distribution plc consolidated balance sheet

As at 31 March 2020

As at 31 March 2020		2020	2019
	Note	£m	£m
ASSETS			
Property, plant and equipment	12	13,224.6	12,587.7
Right-of-use asset	13	10.0	-
Investment property	14	30.1	32.5
Intangible assets	15	1,298.3	1,292.9
Investments	16	161.9	154.9
Trade and other receivables	18	2.0	6.0
Derivative financial instruments	25	156.0	97.4
Retirement benefit assets	27	595.2	105.5
Non-current assets		15,478.1	14,276.9
Inventories	17	38.5	24.2
Trade and other receivables	18	307.8	292.8
Derivative financial instruments	25	7.5	5.5
Cash at bank and in hand	19	201.0	142.7
Current assets	17	554.8	465.2
Total assets	3	16,032.9	14,742.1
LIABILITIES			
Loans and other borrowings	22	426.2	263.5
Trade and other payables	20	601.7	580.3
Lease liabilities	21	1.5	_
Current tax liabilities		0.6	28.2
Derivative financial instruments	25	4.9	2.8
Provisions	28	10.4	11.0
Current liabilities		1,045.3	885.8
Net current liabilities		(490.5)	(420.6)
Towns of advantages in a	22	(111.0	5.010.5
Loans and other borrowings	22	6,111.0	5,919.5
Deferred tax liabilities	26	785.5	592.2
Trade and other payables	20	2,588.7	2,481.6
Lease liabilities	21	8.6	150.2
Provisions	28	208.0	150.3
Non-current liabilities		9,701.8	9,143.6
Total liabilities	3	10,747.1	10,029.4
Net assets		5,285.8	4,712.7
EQUITY			
Share capital	29	1,657.6	1,657.6
Merger reserve	30	(963.1)	(963.1)
Hedging reserve	30	1.2	(5.2)
Retained earnings	30	4,590.1	4,023.4
Total equity		5,285.8	4,712.7

The financial statements on pages 45 to 107 were approved and authorised for issue by the Board of Directors on 23 July 2020 and signed on its behalf by:

P Swift Chief Executive I R Williams Finance Director

	Note	2020 £m	2019 £m
Operating activities - continuing operations		548.6	604.5
Profit for the year		340.0	004.3
Adjustments to reconcile profit for the year to net cash flow			
from operating activities:		201.1	128.7
Income tax expense Finance costs		201.1 299.0	286.9
Finance revenue	_	(11.5)	(10.2)
Depreciation of property, plant and equipment	5	240.8	227.7
Amortisation of customers' contributions	5	(46.1)	(45.3)
Amortisation of intangible assets	5	7.4	5.4
Gain on disposal of property, plant and equipment		(0.3)	(4.8)
Gain on disposal of investment properties		(0.1)	(0.3)
Fair value gains on investment properties		(0.2)	(1.5)
Fair value losses on investment properties		1.5	1.0
Difference between pension contributions paid and amounts			
recognised in the income statement		(150.5)	(139.4)
Increase in provisions		5.6	5.6
Working capital adjustments:			
(Increase)/decrease in inventories		(14.3)	0.5
(Increase)/decrease in trade and other receivables		(11.0)	27.6
Increase in trade and other payables		0.9	22.4
Interest paid		(299.5)	(252.1)
Interest received		12.0	10.7
Customers' contributions received*		158.1	150.1
Income taxes paid		(104.3)	(74.0)
Net cash from operating activities		837.2	943.5
Investing activities			
Purchase of property, plant and equipment		(864.6)	(851.5)
Proceeds from sale of property, plant and equipment		0.9	6.2
Proceeds from sale of investment properties		0.4	3.3
Purchase of intangible assets		(12.0)	(16.5)
Net cash used in investing activities		(875.3)	(858.5)
Financing activities			
Net increase/(decrease) in short-term borrowings		9.0	(189.1)
Payment of lease liabilities		(1.5)	
Proceeds from long-term borrowings		296.7	377.9
Issue costs of long-term borrowings		<b>(1.7)</b>	(2.5)
Dividends paid		(200.1)	(300.2)
Net cash from/(used) in financing activities		102.4	(113.9)
Net increase/(decrease) in cash and cash equivalents		64.3	(28.9)
Cash at bank and in hand at beginning of year	19	123.2	152.1
Cash at bank and in hand at end of year	19	187.5	123.2

<sup>\*</sup>Contributions received from customers towards the cost of capital projects have been reclassified from investing to operating because the underlying nature of the cash inflow is from the business' ongoing regular activities.

For the year ended 31 March 2020

#### 1. Significant accounting policies

The financial statements of Western Power Distribution plc (the "Company") and its subsidiaries (the "WPD Group" or "WPD") for the year ended 31 March 2020 were authorised for issue by the Board of Directors on 23 July 2020 and the balance sheet was signed on the Board's behalf by P Swift and IR Williams. The Company is a public limited company, limited by shares and incorporated and registered in England and Wales. The address of the Company's registered office is stated on page 118.

#### Basis of preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and in accordance with the provisions of the UK Companies Act 2006. The financial statements have also been prepared in accordance with IFRS adopted by the European Union and therefore the WPD Group financial statements comply with Article 4 of the EU IAS regulation. The accounting policies that follow have been consistently applied to all years presented.

The financial statements have been prepared on the historical cost basis, except for the revaluation of investment properties and financial instruments that are measured at revalued amounts or fair values at the end of each reporting period, as explained in the accounting policies below. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or liability, the WPD Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these consolidated financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2, leasing transactions that are within the scope of IFRS 16, and measurements that have some similarities to fair value but are not fair value such as net realisable value in IAS 2 or value in use in IAS 36.

These consolidated financial statements are presented in sterling as this is the currency of the primary economic environment in which the WPD Group operates. All values are rounded to the nearest hundred thousand pounds except when otherwise indicated.

The Comparative financial information has been presented on the same as basis as current year financial information and statement of cash flows has been restated in relation to reclassification of customer contribution from investing activities to operating activities. Contributions received from customers towards the cost of capital projects have been reclassified from investing activities to operating activities because the underlying nature of the cash inflow is from the business' ongoing regular activities.

The significant accounting policies and critical accounting judgements, estimates and assumptions of the WPD Group are set out below.

#### Going concern

The directors have prepared the financial statements on a going concern basis as they have a reasonable expectation that the WPD Group has adequate resources to continue in operational existence for the foreseeable future. This is discussed further under 'financial risk management objectives and policies' within the Directors' report (page 32).

# Basis of consolidation

The WPD Group financial statements consolidate the financial statements of the Company and the entities it controls (its subsidiaries) drawn up to 31 March each year. Control of an investee exists when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To have power over an investee, the investor must have existing rights that give it the current ability to direct the relevant activities of the investee. Subsidiaries, other than those acquired under common control transactions, are consolidated from the date of their acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of subsidiaries are prepared for the same reporting year as the parent Company, using consistent accounting policies. Intercompany balances and transactions, including unrealised profits arising from intragroup transactions, have been eliminated. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the assets transferred.

For business combinations involving entities under common control, the pooling of interest method is applied. The assets and liabilities of the combining entities are reflected at their carrying amounts. No adjustments are made to reflect fair values, or recognise any new assets or liabilities, at the date of the combination that would otherwise be done under the acquisition method. The only adjustments that are made are to harmonise accounting policies. No 'new' goodwill is recognised as a result of the combination. The only goodwill that is recognised is any existing goodwill relating to the combining entities. Any difference between the consideration paid/transferred and the equity 'acquired' is reflected within equity. The income statement reflects the results of the combining entities for the full year, irrespective of when the combination took place.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

# Impact of new International Financial Reporting Standards

The Group has applied the following standards and amendments, effective for an annual period that begins on or after 1 January 2019, for the first time for their annual reporting period commencing 1 April 2019:

- IFRS 16 "Leases";
- Prepayment Features with Negative Compensation Amendments to IFRS 9;
- Long-term Interests in Associates and Joint Ventures Amendments to IAS 28;
- Annual Improvements to IFRS Standards 2015 2017 Cycle;
- Plan Amendment, Curtailment or Settlement Amendments to IAS 19;
- IFRIC 23 "Uncertainty over Income Tax Treatments".

Except as defined below in relation to IFRS 16, the Group has concluded that these standards do not have any material impact on the Group's financial statements.

#### **IFRS 16**

IFRS 16 "Leases" supersedes the previous lease guidance including IAS 17 "Leases" and the related interpretations and is effective for accounting periods beginning on or after 1 January 2019. IFRS 16 provides comprehensive guidance for the identification of lease arrangements for both lessee and lessor and a new model for lessee accounting in which all leases, other than short-term and small-ticket-item leases, are accounted for by the recognition on the balance sheet of a right-to-use asset and a lease liability, and the subsequent amortisation of the right-to-use asset and unwinding of the lease liability using an appropriate discount rate over the lease term

The Group has adopted IFRS 16 retrospectively with effect from 1 April 2019 but has elected not to restate comparatives on initial adoption, as permitted within the Standard.

#### (i) Impact of the new definition of lease

The Group has made use of the practical expedient available on transition to IFRS 16 not to reassess whether a contract is or contains a lease. Accordingly, the definition of a lease in accordance with IAS 17 and IFRIC 4 will continue to be applied to those contracts entered or modified before 1 April 2019. The change in definition of a lease mainly relates to the concept of control. IFRS 16 determines whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time in exchange for consideration. This is in contrast to the focus on 'risks and rewards' in IAS 17. The Group applies the definition of a lease and related guidance set out in IFRS 16 to all contracts entered into or changed on or after 1 April 2019.

# (ii) Measurement of lease liabilities

On adoption of IFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17. These liabilities were measured at the present value of the remaining lease payments, discounted using the Group's incremental borrowing rate as of 1 April 2019. The weighted average incremental borrowing rate applied to the lease liabilities on 1 April 2019 was 3.22%.

In accordance with the relevant provisions of the Standard, the Group has elected not to recognise short term leases and low value leases on the balance sheet. The lease payments associated with these leases are recognised as an expense on a straight line basis over the lease term.

In measuring the initial lease liability, the Group has also adopted the practical expedient for accounting for operating leases with a remaining lease term of less than 12 months as at the application date as short-term leases.

	2020 £m
Operating lease commitments as disclosed as at 31 March 2019	18.3
Operating lease commitments at 31 March 2019 discounted using incremental borrowing rate	10.8
Lease liability recognised as at 1 April 2019	10.8

# (iii) Measurement of right-of-use asset

Right-of-use assets are measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the balance sheet as at 31 March 2019. The right-of-use assets recognised as at 1 April 2019 amount to £10.8m.

For the year ended 31 March 2020

# 1. Significant accounting policies (continued)

# Impact of new International Financial Reporting Standards (continued)

# IFRS 16 (continued)

#### (iv) Retained earnings impact

There is no retained earnings impact on the initial transition to IFRS 16, since the right-of-use assets are measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments.

#### (v) Lessor accounting

The adoption of IFRS 16 did not result in any changes to the accounting for operating leases as a lessor.

(vi) Impact of adoption of IFRS 16 on the balance sheet as at 31 March 2020

(vi) Impact of adoption of IFRS 10 on the balance sheet as at 31 March 2020	2020 £m
Right-of-use-assets	10.0
Lease liabilities - current	(1.5)
Lease liabilities - non-current	(8.6)
(vii) Impact of adoption of IFRS 16 on the income statement for the year ended 31 March 2020	
(, <sub>1</sub> <sub>3</sub> <sub>1</sub> <sub>1</sub>	2020
	£m
Depreciation of right-of-use assets	(1.3)
Interest payable on lease liabilities	(0.3)
Operating rent expense	1.5
Net impact on profit before tax	(0.1)

(viii) Impact of adoption of IFRS 16 on the statement of cash flows for the year ended 31 March 2020

Under IAS 17, all lease payments for operating leases were presented as part of cash flows from operating activities. On adoption of IFRS 16, the Group recognises cash flows pertaining to leases as below:

- Short term lease payments and payments for low value leases are recognised as part of operating activities;
- Cash payments for the interest portion of the lease liabilities are recognised as part of operating activities; and
- Cash payments for the principal portion of the lease liabilities are recognised as part of financing activities.

Consequently, the net cash generated by operating activities has increased by £1.5m, being the lease payments, and net cash used in financing activities has increased by the same amount.

The adoption of IFRS 16 did not have an impact on net cash flows.

The EU has adopted IFRS 16 with effect from 1 January 2019.

#### Not yet adopted

The following pronouncements from the International Accounting Standards Board will become effective for future financial reporting periods and have not yet been adopted by the WPD Group:

- Amendments to IFRS 3 " Definition of a Business" effective for annual periods beginning on or after 1 January 2020.
- Amendments to IAS 1 and IAS 8 " Definition of material" effective for annual periods beginning on or after 1 January 2020.
- Amendments to IFRS 9, IAS 39 and IFRS 7, Interest Rate Benchmark Reforms effective for annual periods beginning on or after 1
   January 2020
- IFRS 17 "Insurance contracts" effective for annual periods beginning on or after 1 January 2021.
- Amendments to IFRS 10 and IAS 28 "Sale or Contribution of Assets between an Investor and its Associate or Joint Venture" effective date yet to be decided.

WPD does not anticipate these standards and interpretations will have a material impact on the Group.

For the year ended 31 March 2020

# 1. Significant accounting policies (continued)

# Business combinations and goodwill

Business combinations, other than the combination of businesses under common control, are accounted for using the acquisition method. The identifiable assets acquired and liabilities assumed are measured at their fair values at the acquisition date. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value, and the amount of any non-controlling interest in the acquiree. Acquisition costs incurred are expensed and included in distribution and administration expenses.

Goodwill is initially measured as the excess of the aggregate of the consideration transferred, the amount recognised for any non-controlling interest and the acquisition-date fair values of any previously held interest in the acquiree over the fair value of the identifiable assets acquired and liabilities assumed at the acquisition date.

At the acquisition date, any goodwill acquired is allocated to each of the cash-generating units, or groups of cash-generating units, expected to benefit from the combination's synergies.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

#### Foreign currencies

Transactions in foreign currencies are initially recorded in the entity's functional currency by applying the spot exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the income statement.

For debt not in sterling, see "Derivative financial instruments and hedging activities" below.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

# Revenue recognition

Distribution Use of System ("DUoS") Revenue

The Group consists of four distribution network operators ("DNOs") in the UK that earn the majority of their revenue from providing distribution use of system services. The services are provided under a Distribution Connection and Use of System Agreements ("DCUSA") with their customers.

There is a single performance obligation under the DCUSA: the DNO is required to use its distribution network to deliver electricity from metered entry points to exit point. WPD's performance obligation of delivering electricity represents a promise to deliver a series of distinct services that should be accounted for as a single performance obligation. The performance obligation is satisfied over time as:

- a) Customers immediately control and consume the benefits WPD provides;
- b) WPD's service does not create or enhance an asset with an alternate use to WPD;
- c) WPD has the right to payment from the customer for the service that has been provided.

WPD measures the progress of the performance obligation using the output method. The output method recognises revenue based on the direct measurements of value transferred to the customer. Accordingly WPD records revenue on a monthly basis, based on the amount of kilowatt hour ("KWH") of electricity delivered.

Revenue includes an assessment of the volume of unbilled energy distributed to customers between the date of the last meter reading and the year-end.

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

#### Finance income

Finance revenue comprises interest receivable on funds invested. Interest income is recognised in the income statement as it accrues, on an effective rate basis.

# Rental income

Rental income arising from operating leases on investment properties is accounted for on a straight line basis over the lease term.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

#### Revenue recognition

# Engineering recharges

Engineering recharges relate to the recovery of costs incurred in relation to construction work requested by customers, such as rerouting of existing network assets. The performance obligation relates to completion of work as per the terms of the contract. The consideration received is recognised as revenue as the construction work is completed.

#### Customer contributions

Contributions receivable in respect of additions to property, plant and equipment for new connections are treated as deferred income, which is credited to the income statement over the estimated weighted life of the related assets of 69 years. The performance obligation for customer contribution contracts is to provide customers with an ongoing network connection and thus is satisfied over a period of time instead of at a point of time. Customers immediately control and consume the benefits WPD provides.

#### Other operating income and expense

Other operating income and expense includes movements in the fair value of investment properties and gains and losses arising on the disposal of properties by the WPD Group's property management business which is considered to be part of the normal recurring operating activities of the WPD Group.

#### Finance costs

Finance expenses comprise interest payable on borrowings, accretion relating to inflation on index linked debt and the release of discounts on provisions. Interest charges are recognised in the income statement as they accrue, on an effective rate basis.

#### Leases

#### WPD Group as a lessee

The Group assesses whether a contract is, or contains, a lease at inception of the contract. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Group recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets (assets with a purchase price of less than £5,000). For these leases, the Group recognises the lease payments as an operating expense on a straight-line basis over the term of the lease.

The lease liability is initially measured at the present value of the unpaid lease payments at the commencement date, discounted by using the Group's incremental borrowing rate.

The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the carrying amount to reflect the lease payments made.

The Group remeasures the lease liability (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- The lease term has changed or there is a significant event or change in circumstances resulting in a change in the assessment of exercise of a purchase option, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.
- The lease payments change due to changes in an index or rate, in which case the lease liability is remeasured by discounting the revised lease payments using an unchanged discount rate (unless the lease payments change is due to a change in a floating interest rate, in which case a revised discount rate is used).
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured based on the lease term of the modified lease by discounting the revised lease payments using a revised discount rate at the effective date of the modification.

The right-of-use assets comprise the initial measurement of the corresponding lease liability, less any lease incentives received and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and impairment losses. Right-of-use assets are depreciated over the shorter period of the lease term and the useful life of the underlying asset.

Variable rents that do not depend on an index or rate are not included in the measurement of the lease liability and the right-of-use asset. The related payments are recognised as an expense in the income statement in the period in which the event or condition that triggers those payments occurs.

For the year ended 31 March 2020

# 1. Significant accounting policies (continued)

#### Leases (continued)

As a practical expedient, IFRS 16 permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The Group has not used this practical expedient. For contracts that contain a lease component and one or more additional lease or non-lease components, the Group allocates the consideration in the contract to each lease component on the basis of the relative stand-alone price of the lease component and the aggregate stand-alone price of the non-lease components.

#### WPD Group as a lessor

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. When the Group is an intermediate lessor, it accounts for the head lease and the sub-lease as two separate contracts. The sub-lease is classified as a finance or operating lease by reference to the right-of-use asset arising from the head lease. The Group has no finance leases.

Assets leased out under operating leases are included in property, plant and equipment and depreciated over the estimated useful lives. Rental income, including the effect of lease incentives, is recognised on a straight line basis over the term of the lease. Lease termination fees are allocated to the income statement upon termination. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

#### Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairments. Borrowing costs directly attributable to assets under construction and which meet the recognition criteria in IAS 23 are capitalised as part of the cost of that asset.

Expenditure on electricity infrastructure assets relating to increases in capacity or enhancements of the network including qualifying replacement expenditure are treated as additions. Other costs incurred in maintaining the operating capability of the network in accordance with defined standards of service are expensed in the year in which the expenditure is incurred.

Cost comprises the aggregate amount paid and the fair value of any other consideration given to acquire the asset and includes costs directly attributable to making the asset capable of operating as intended. Employee costs incurred in implementing the capital schemes of the WPD Group are capitalised within infrastructure assets together with the cost of materials and an appropriate proportion of overheads.

Contributions received towards the cost of property, plant and equipment which include low carbon network funding are included in trade and other payables as deferred income and credited on a straight-line basis to the income statement over the estimated economic useful lives of the assets to which they relate.

Depreciation is provided on all property, plant and equipment, other than land, on a straight-line basis over its expected useful life as follows:

	<u>Years</u>
Distribution network assets:	
Overhead lines and poles	65
Underground cables	85
Plant and machinery (transformers and switchgear)	55
Meters	3
Other (towers and substation buildings)	Up to 80
Buildings - freehold	Up to 60
Buildings - long leasehold	Up to 60
Fixtures and equipment	Up to 20
Vehicles and mobile plant	Up to 10

The carrying values of property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable, and are written down immediately to their recoverable amount. Useful lives and residual values are reviewed annually and where adjustments are required these are made prospectively.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the derecognition of the asset is included in the income statement in the period of derecognition.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

#### Investment property

Investment properties are measured initially at cost, including transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met; and excludes the costs of day to day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the reporting date and the highest and best use. Gains or losses arising from changes in the fair values of investment properties are included in the income statement in the period in which they arise.

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal.

The difference between the net disposal proceeds and the carrying amount of the asset is recognised in the income statement in the period of derecognition.

Transfers are made to or from investment property only when there is a change in use. For a transfer from investment property to owner occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner occupied property becomes an investment property, the WPD Group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

#### Intangible assets

Intangible assets, other than goodwill, include customer contracts and computer software and are stated at the amount initially recognised, less accumulated amortisation and accumulated impairment losses.

Intangible assets acquired separately from a business are carried initially at cost. The initial cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset. An intangible asset acquired as part of a business combination is measured at fair value at the date of acquisition and is recognised separately from goodwill if the asset is separable or arises from contractual or other legal rights.

Intangible assets with a finite life are amortised on a straight-line basis over their expected useful lives. The expected useful lives of assets are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

#### Contracts

The value recognised for customer contracts relating to acquired telecommunications activities is amortised over the period of the contracts. It is subject to an impairment test at least on an annual basis. It is written off if the activity is sold.

# Computer software

Costs directly associated with the development of computer software for internal use are capitalised where technical feasibility can be demonstrated, the WPD Group is satisfied that future economic benefits will flow to the WPD Group and the cost can be separately identified and reliably measured. Software is measured initially at cost and amortised on a straight-line basis over its estimated useful life. The carrying amount is reduced by any provision for impairment where necessary. The estimated useful life assigned to computer software is up to five years.

# Impairment of property, plant and equipment, intangible assets, and goodwill

The WPD Group assesses goodwill and intangibles with indefinite useful lives for impairment annually and other assets or groups of assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If any such indication of impairment exists, the Group makes an estimate of the asset's recoverable amount. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. An asset group's recoverable amount is the higher of its fair value less costs of disposal and its value in use. Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount.

The business plan, which is approved on an annual basis by senior management, is the primary source of information for the determination of value in use. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

# Impairment of property, plant and equipment, intangible assets, and goodwill (continued)

Fair value less costs of disposal is the price that would be received to sell the asset in an orderly transaction between market participants and does not reflect the effects of factors that may be specific to the entity and not applicable to entities in general. For acquisition purposes, the value of a regulated DNO is usually seen as the RAV plus a premium. The premium takes into consideration WPD's performance and any recent market transactions.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such an indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in profit or loss. After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate the recoverable amount of the group of cash-generating units ("CGUs") to which the goodwill relates should be assessed. In assessing whether goodwill has been impaired, the carrying amount of the group of CGUs (including goodwill) is compared with their recoverable amount. The recoverable amount of a group of CGUs to which goodwill is allocated is the higher of value in use and fair value less costs of disposal. Where the recoverable amount of the group of CGUs to which goodwill has been allocated is less than the carrying amount, an impairment loss is recognised. An impairment loss recognised for goodwill is not reversed in a subsequent period.

The WPD Group records all assets and liabilities acquired in purchase acquisitions, including goodwill, at fair value. Goodwill is not amortised but is subject, at a minimum, to annual tests for impairment. The initial goodwill recorded and subsequent impairment analysis require management to make subjective judgements concerning the recoverable amount of cash-generating units, specifically in relation to cash flows, discount rate and estimated fair value less cost to dispose. At 31 March 2020, the carrying value of goodwill amounted to £1,254.1m (2019: £1,254.1m).

Fair value less cost to dispose is determined based on an implied premium applied to the RAV. RAV is a generally accepted and widely used industry method for measuring asset value and as such is considered an adequate proxy of the fair value less cost to dispose. Implied premium is estimated in accordance with latest available market information, industry prospects, WPD's current performance and future plans.

# Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. It excludes borrowing costs.

# Taxation

The income tax expense (or credit) for the period comprises current and deferred tax. Income tax is recognised in the income statement unless it relates to an item that has been recognised in other comprehensive income, in which case it is also recognised in other comprehensive income.

Current tax is measured at the amount expected to be payable (or recoverable) in respect of the taxable profit (or loss) for the period based on tax rates and laws that have been enacted or substantively enacted at the balance sheet date. This includes UK corporation tax payable to HM Revenue & Customs ("HMRC") and amounts payable to (or receivable from) other UK Group companies for losses and other amounts transferred between them ("group relief").

Deferred tax is the tax expected to be payable (or recoverable) in future periods due to differences between the time when profits and losses are recognised in the financial statements and the time when those profits and losses are included in tax returns filed with HMRC. These temporary differences arise in the current period and then reverse in future periods. The temporary differences are calculated by comparing the carrying value of assets and liabilities at the balance sheet date with their corresponding tax bases included in tax returns.

Deferred tax is recognised on all temporary differences except:

• where the temporary difference arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss;

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

#### Taxation (continued)

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future; and
- deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the asset may be recovered.

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods when the temporary differences will reverse based on tax rates and laws that have been enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are offset only to the extent permitted by tax legislation.

#### Pension benefits

The WPD Group operates four defined benefit pension plans, all of which require contributions to be made to separately administered funds. The larger plans are the two unitised sections of the industry-wide Electricity Supply Pension Scheme ("ESPS"). The ESPS scheme is, with very limited exception, closed to new members. A defined contribution plan is offered to new employees. The final two plans, which are also closed to new members and have no active employees, are the Western Power Utilities Pension Scheme ("WPUPS") and the much smaller Infralec 1992 Scheme. WPD also has an unfunded obligation which relates to previous executives of WPD East Midlands and WPD West Midlands.

The cost of providing benefits under the defined benefit plans is determined separately for each plan using the projected unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of defined benefit obligation) and is based on actuarial advice. Past service costs, resulting from either a plan amendment or a curtailment (a reduction in future obligations as a result of a material reduction in the plan membership), are recognised immediately when the WPD Group becomes committed to a change. The current service cost (including administration costs) is allocated to the income statement or capital expenditure as appropriate.

Net interest expense related to pension benefits represents the net change in the present value of plan obligations and the value of plan assets resulting from the passage of time, and is determined by applying the discount rate to the present value of the benefit obligation at the start of the year and to the fair value of plan assets at the start of the year, taking into account expected changes in the obligation or plan assets during the year. Net interest expense relating to pension benefits is recognised in the income statement.

Remeasurements of the net defined benefit liability or asset, comprising actuarial gains or losses, and the return on plan assets (excluding amounts included in net interest described above) are recognised within other comprehensive income in the period in which they occur.

The retirement benefit obligation or asset recognised in the balance sheet represents the deficit or surplus in the WPD Group's defined benefit pension plan. Surplus or deficit comprises the total of the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds), less the fair value of plan assets out of which the obligations are to be settled directly. Fair value is based on market price information and in the case of quoted securities is the published bid price. Any surplus resulting from this calculation is limited to the present value of any economic benefits available in the form of a reduction in future contributions to the schemes.

Contributions to defined contribution schemes are recognised in the income statement or capital expenditure as appropriate in the year in which they become payable.

#### Share-based payments

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

#### **Provisions**

A provision is recognised when the WPD Group has a legal or constructive obligation as a result of a past event; it is probable that an outflow of economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation. If the effect is material, expected future cash flows are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability.

For the year ended 31 March 2020

# 1. Significant accounting policies (continued)

#### Dividend distribution

Dividend distribution to the Company's shareholder is recognised as a liability in the WPD Group's financial statements in the year in which the dividends are approved by the Company's directors.

#### Financial assets

Financial assets are classified as debt instruments at amortised cost; debt instruments at fair value through other comprehensive income ("FVOCI"); financial assets at fair value through profit and loss ("FVTPL"); derivatives designated as hedging instruments in an effective hedge; or as equity instruments designated at FVOCI, as appropriate. Financial assets include cash at bank and in hand, trade and other receivables, investments at amortised cost, and derivative financial instruments. The WPD Group determines the classification of its financial assets at initial recognition. Financial assets are recognised initially at fair value, normally being the transaction price plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs. For financial assets at FVTPL, transaction costs are immediately recognised in the income statement.

The subsequent measurement of financial assets depends on their classification, as follows:

#### Debt instruments at amortised cost

Debt instruments that meet the hold-to-collect business model test and sole payment principal and interest ("SPPI") contractual cash flow test are carried at amortised cost using the effective interest method, if the time value of money is significant. Gains and losses are recognised in income when the debt instruments are derecognised or impaired, as well as through the amortisation process. This category of financial assets includes cash at bank and in hand excluding the short term deposits, trade and other receivables including accrued income and investment at amortised cost.

#### Financial assets at FVTPL

Financial assets at FVTPL are carried on the balance sheet at fair value with gains or losses recognised in the income statement. Short term deposits are included in this category. Short term deposits are highly liquid short term investments that are readily convertible to known amounts of cash and are subject to insignificant risk of changes in value.

#### Financial assets at FVOCI

Financial assets at FVOCI, that meet the sole payment principal and interest ("SPPI") contractual cash flow test and the objective of the group is achieved both by collecting contractual cash flows and selling financial assets, are carried on the balance sheet at fair value with gains or losses recognised in other comprehensive income. This category of financial assets include derivatives designated as hedging instruments in an effective cash flow hedge.

Derivatives designated as hedging instruments in an effective hedge

These derivatives are carried on the balance sheet at fair value. The treatment of gains and losses arising from revaluation is described below in the accounting policy for derivative financial instruments and hedging activities.

#### Impairment of financial assets

WPD recognises impairment on financial assets following the expected credit loss ("ECL") model in IFRS 9.

Critical to the determination of ECL is the definition of default. The definition of default is used in measuring the amount of ECL, as default is a component of the probability of default ("PD") which affects the measurements of ECLs. WPD constitutes the following as an event of default:

- (i) Borrower is past due by more than 90 days on any material credit obligation to the Group; or
- (ii) Borrower is unlikely to pay its credit obligation to the Group in full

WPD has the following financial assets not measured at FVTPL that are subject to ECL:

Trade and other receivables including accrued income

WPD applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all receivables. Lifetime ECLs result from all possible default events over the life of financial instruments.

To measure the expected credit losses, trade and other receivables have been grouped based on shared risk characteristics and the days past due. Accrued income is effectively a receivable as well for the purposes of the expected credit loss model since it is unbilled only because a passage of time is required. WPD has therefore concluded that expected loss rates for trade receivables are a reasonable approximation of the loss rates for accrued income as well.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

#### Impairment of financial assets (continued)

Trade and other receivables including accrued income (continued)

The expected credit loss rates are primarily based on historical credit losses experienced. The historical loss rates are then adjusted for forward looking information on macroeconomic factors affecting the customer's ability to pay. The general economy trends and conditions impact the customers ability to pay. Another key factor to consider is the liquidity and overall financial position of the key electricity suppliers.

Trade and other receivables are written off when there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include, amongst others, the failure of the debtor to engage in a repayment plan, and a failure to make payments for a period greater than 120 days past due.

#### Investments at amortised cost

Investments at amortised cost is considered to be low risk, and therefore the impairment provision is determined as 12 months expected credit loss. Twelve month ECL results from those default events on the financial assets that are possible within 12 months after the reporting date.

#### Cash at bank and in hand

This comprises cash at bank, in hand and short term deposits. Since short term deposits are FVTPL, they are not subject to the impairment requirements of IFRS 9. Whereas cash at bank and in hand is subject to the impairment requirements of IFRS 9 but the impairment loss on these is deemed immaterial since they have an insignificant risk of change in value.

#### Cash and cash equivalents

In the consolidated cash flow statement and related notes, cash and cash equivalents includes cash at bank and in hand and short term deposits which are readily convertible into known amounts of cash and have a maturity of three months or less and which are subject to an insignificant risk of change in value, net of any bank overdrafts which are payable on demand.

#### Financial liabilities

Financial liabilities are classified as financial liabilities at FVTPL; or as financial liabilities measured at amortised cost, as appropriate. Financial liabilities include trade and other payables including accruals and loans and other borrowings. The WPD Group determines the classification of its financial liabilities at initial recognition. The measurement of financial liabilities depends on their classification, as follows:

# Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss are carried on the balance sheet at fair value with gains or losses recognised in the income statement. Derivatives, other than those designated as effective hedging instruments, are included in this category.

# Financial liabilities measured at amortised cost

All other financial liabilities are initially recognised at fair value. For interest-bearing loans and borrowings this is the fair value of the proceeds received net of issue costs associated with the borrowing.

After initial recognition, other financial liabilities are subsequently measured at amortised cost. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in interest and other income and finance costs.

This category of financial liabilities includes trade and other payables and loans and other borrowings.

# Derivative financial instruments and hedging activities

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

Gains or losses arising from changes in the fair value of derivatives that are not designated as effective hedging instruments are recognised in the income statement. For the purpose of hedge accounting, hedges are classified as:

- Cash flow hedges when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a
  recognised asset or liability or a highly probable forecast transaction; or
- Fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment.

For the year ended 31 March 2020

#### 1. Significant accounting policies (continued)

# Derivative financial instruments and hedging activities (continued)

Hedge relationships are formally designated and documented at inception, together with the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged, and how the entity will assess the hedging instrument effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected at inception to be highly effective in achieving offsetting changes in fair value or cash flows. Hedges meeting the criteria for hedge accounting are accounted for as follows:

# Cash flow hedges

For cash flow hedges, the effective portion of the gain or loss on the hedging instrument is recognised directly as other comprehensive income in the net unrealised gains reserve, while the ineffective portion is recognised in the income statement. Amounts taken to other comprehensive income are transferred to the income statement when the hedged transaction affects the income statement, such as when a forecast sale or purchase occurs. Where the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If a forecast transaction is no longer expected to occur, amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in other comprehensive income remain in equity until the forecast transaction occurs and are transferred to the income statement or to the initial carrying amount of a non-financial asset or liability as above. If the related transaction is not expected to occur, the amount is taken to the income statement.

#### Fair value hedges

The WPD Group did not have any fair value hedges during the years presented in these financial statements.

#### Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The Group categorises assets and liabilities measured at fair value into one of three levels depending on the ability to observe inputs employed in their measurement. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are inputs that are observable, either directly or indirectly, other than quoted prices included within Level 1 for the asset or liability. Level 3 inputs are unobservable inputs for the asset or liability reflecting significant modifications to observable related market data or the WPD Group's assumptions about pricing by market participants.

# Offsetting of financial assets and liabilities

Financial assets and liabilities are presented gross in the balance sheet unless both of the following criteria are met: the Group currently has a legally enforceable right to set off the recognised amounts; and the Group intends to either settle on a net basis or realise the asset and settle the liability simultaneously. A right of set off is the Group's legal right to settle an amount payable to a creditor by applying against it an amount receivable from the same counterparty. The relevant legal jurisdiction and laws applicable to the relationships between the parties are considered when assessing whether a current legally enforceable right to set off exists.

# **Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily take a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective assets. All other borrowing costs are expensed in the period in which they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

### 2. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in Note 1, the directors are required to make judgements (other than those involving estimates) that have a significant impact on the amounts recognised and to make 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 period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

For the year ended 31 March 2020

#### 2. Critical accounting judgements and key sources of estimation uncertainty (continued)

#### Critical judgements in applying the Group's accounting policies

The following are the critical judgements, apart from those involving estimations (which are dealt with separately below), that the directors have made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

#### Capitalisation of overheads - Nature of costs capitalised

Amounts capitalised as network assets include indirect costs associated with the engineering department and an element of corporate overhead costs. The costs are initially expensed to the income statement with a portion being capitalised based on management's assessment of the costs incurred that are directly linked to the capital work performed. The nature of costs to be included for capitalisation is a key judgement and is based on an analysis of the activities directly attributable to capital work. During the current year, following a detailed management review, certain costs are no longer deemed directly attributable to capital work and have therefore been excluded from capitalisation.

#### *Uncertain tax positions*

The Group's current tax expense and current tax liability reflect management's best estimate and judgement regarding the amount of UK corporation tax payable for the current and previous periods that remains to be agreed with HMRC. The UK tax legislation contains detailed and complex rules which are regularly updated. Management monitors any changes to the UK tax legislation and assesses their impact on the Group's tax position. In particular, the OECD Base Erosion and Profit Shifting ("BEPS") project resulted in the Government enacting complex legislation relating to the amount of finance costs that may be deducted from taxable profits, such as the Corporate Interest Restriction rules and the Hybrid and other mismatches rules, for both of which HMRC guidance and practical experience is still developing. Some of these rules may not directly apply to the Group, but apply to finance costs of PPL affiliate companies which may impact the amount of group relief available to the Group. Management has assessed the impact of this legislation on the Group's tax position and has taken necessary actions to ensure that the Group is compliant with the rules.

Management evaluates uncertain tax items which are subject to interpretation and agreement of the position with HMRC which, due to the complexity of the matters, may not be reached for a number of years. Management uses its judgement to determine the expected amount of finance costs that may be deducted, taking into account any progress in discussions with HMRC, together with in-house and third party advice on the potential outcome and recent developments in case law, tax authority practices and previous experience. The amount that may ultimately be deducted upon agreement with HMRC may differ to that recorded in the financial statements, but management does not expect that any adjustments would have a material impact on the Group's financial results and positions.

# Goodwill - nature of cash flows

For purposes of goodwill impairment, cash flows to be included in determining the value in use of a cash generating unit ("CGU") is a key judgement. IAS 36 "Impairment of assets" requires that cash flows for value in use calculations shall only include cash flows for a CGU in its current condition. All cash flows in relation to reinforcement work, or alternatives to reinforcement work such as flexible projects, as per the approved business plan, are considered as cash flows necessary to operate and maintain the networks in their current condition and are therefore included for the purposes of determining the value in use of the CGU.

#### Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting period that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

### Capitalisation of overheads - capitalisation rate

Amounts capitalised as network assets include indirect costs associated with the engineering department and an element of corporate overhead costs. The costs are initially expensed to the income statement with a portion being capitalised using an appropriate rate.

In previous years the rate of capitalisation has been based on the analysis of total labour costs, as split between capital and revenue activities. In the current year, following a detailed management review, certain costs are no longer considered directly attributable to capital work and the capitalisation rate for some costs has been based on an analysis of total costs, as split between capital and revenue activities. The net impact of these changes on the overall capitalisation of overheads is immaterial.

The rate is reviewed in detail annually and a reasonableness test is performed in light of total capital spend during the year. The total amount of overheads capitalised at 31 March 2020 is £73.5m (2019: £73.4m). Information on sensitivity to the rate is as below:

For the year ended 31 March 2020

#### 2. Critical accounting judgements and key sources of estimation uncertainty (continued)

Key sources of estimation uncertainty (continued)

Capitalisation of overheads - capitalisation rate (continued)

•	J	•	·	,			2020	2019
							Income	Income
							statement	statement
							(before tax)	(before tax)
							+/ <b>- £m</b>	+/- £m
Change in	rate +/- 1%						1.1	1.2
Change in	rate +/- 5%						5.5	6.0

#### Pension obligations

The WPD Group has a commitment, mainly through the Electricity Supply Pension Scheme ("ESPS"), to pay pension benefits. The costs of these benefits and the present value of the WPD Group's pension liabilities depend on such factors as the life expectancy of the members, the salary progression of current employees which is based on inflation rate and the discount rate at which the future pension payments are discounted. Based on advice from external actuaries, WPD uses estimates for all these factors in determining the pension costs and liabilities incorporated in the financial statements. The assumptions reflect historical experience and management's judgement regarding future expectations.

The discount rate used is based on the interest rates of relevant high quality corporate bonds. The increase in discount rates due to the global COVID-19 outbreak has been accompanied by a fall in inflation expectations, thus resulting in an overall surplus on the Group's defined benefit schemes of £599.5m (2019: £110.1m).

The long term mortality rates may also be impacted to some extent by COVID-19 but due to uncertainty surrounding the outbreak, the impact is currently unclear and therefore has been excluded from life expectancy assumptions used in the valuation of pension liabilities.

In light of the COVID-19 pandemic, the valuation of certain pension assets has been identified as an additional area of estimation uncertainty that impacts the Group's position as at 31 March 2020. Due to uncertainty in the markets, property valuations by independent valuers have been reported on the basis of material valuation uncertainty in line with current industry practice. The balance of pension assets invested in property/real estate funds amounts to £402.3m, which represents 6% of total pension assets. The aggregate surplus of the defined benefit plans is sufficient to cover the loss, if any, on the long term value of property assets.

See Note 27 for further details and information on sensitivities.

#### Goodwill

The WPD Group records all assets and liabilities acquired in purchase acquisitions, including goodwill, at fair value. Goodwill is not amortised but is subject, at a minimum, to annual tests for impairment. Following the assessment of the recoverable amount of goodwill allocated to the East Midlands, West Midlands and South Wales, to which goodwill of £518.8m, £614.4m and £120.9m has been allocated respectively, the directors consider the recoverable amount of goodwill allocated to these CGUs to be most sensitive to the pre-tax discount rate of 5.00% (2019: 4.84%), the assumed terminal value multiple of 35% (2019: 25%) applied to the RAV on the assumed exit date at 31 March 2028 and key future RIIO-ED2 price control assumptions including the cost of equity allowance and incentive revenues. The discount rate reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. Whilst the Group has some certainty over the future cash flows generated by the assets in the current RIIO-ED1 price control period there is less certainty over the future RIIO-ED2 price control period and in particular the cost of equity allowance and incentive revenues; these factors are partly taken into account in the discount rate calculation.

The sensitivity analysis in respect of the recoverable amounts of the CGUs allocated to goodwill are presented in Note 15.

#### 3. Operating segment information

The WPD Group's operating segments are those used internally by the Board of Directors to run the business, allocate resources and make strategic decisions. The WPD Group's reportable segments are the regulated distribution of electricity in the South West, East Midlands and West Midlands of England and South Wales, and other businesses. Distribution involves the delivery of electricity across the WPD Group's distribution network. Other businesses relate to non-regulated activities including telecommunications, property management and helicopter operations which principally support the main business, and metering.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies.

For the year ended 31 March 2020

# 3. Operating segment information (continued)

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss on the same basis as in the consolidated financial statements. However, WPD Group financing (including finance costs and finance income) and income taxes are managed on a group basis and are not allocated to operating segments.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties. Segment revenue, segment expense and segment results include transfers between business segments. Those transfers are eliminated on consolidation.

Analysis of revenue, operating profit, and assets and liabilities by segment is provided below. Substantially all revenues and profit before tax arise from operations within the UK.

a) Revenues	<b>Total revenue</b>		Inter-segment revenue		External revenue	
	2020	2019	2020	2019	2020	2019
	£m	£m	£m	£m	£m	£m
Distribution network systems						
South West	381.7	372.2	( <b>0.4</b> )	(0.8)	381.3	371.4
South Wales	263.6	259.2	(0.1)	(0.2)	263.5	259.0
East Midlands	526.3	506.2	(0.4)	(0.1)	525.9	506.1
West Midlands	525.4	524.7	(0.3)	(0.2)	525.1	524.5
	1,697.0	1,662.3	(1.2)	(1.3)	1,695.8	1,661.0
Other businesses	59.6	58.1	(31.9)	(33.5)	27.7	24.6
	1,756.6	1,720.4	(33.1)	(34.8)	1,723.5	1,685.6

#### **Information about major customers**

Revenues from the WPD Group's largest five customers amounted to £275.0m, £220.9m, £214.6m, £209.0m and £183.5m (2019: £266.8m, £231.4m, £227.2m, £226.9m and £219.3m) arising from sales reported across the South West, South Wales, East Midlands and West Midlands segments.

# b) Segment profit

	2020	2019
	£m	£m
Distribution network systems		
South West	222.7	217.9
South Wales	159.1	154.6
East Midlands	335.8	319.6
West Midlands	334.8	329.2
	1,052.4	1,021.3
Other businesses	8.1	10.6
Corporate and unallocated*	(23.3)	(22.0)
Operating profit	1,037.2	1,009.9
Finance revenue	11.5	10.2
Finance costs	(301.0)	(282.6)
Net finance income/(expense) relating to pensions and other post-retirement benefits	2.0	(4.3)
Profit before tax	749.7	733.2
Taxation		
South West	(44.8)	(29.1)
South Wales	(31.8)	(18.4)
East Midlands	(66.1)	(40.8)
West Midlands	(65.3)	(40.3)
Other businesses	6.9	(0.1)
	(201.1)	(128.7)
Profit for the year attributable to equity holders of the parent	548.6	604.5

<sup>\*</sup> Corporate and unallocated comprises primarily current service pension costs (net of capitalisation).

# 3. Operating segment information (continued)

# c) Assets, liabilities, and capital expenditure

	Segment assets (i)		Segment liabilities (ii)		Capital expenditure (iii)	
	2020	2019	2020	2019	2020	2019
	£m	£m	£m	£m	£m	£m
Distribution network systems						
South West	3,080.0	2,895.8	692.5	655.4	235.5	219.5
South Wales	2,175.8	2,076.6	451.8	433.6	139.2	148.7
East Midlands	4,934.1	4,712.6	1,161.7	1,112.5	298.9	279.2
West Midlands	4,600.4	4,426.7	805.2	772.7	255.3	247.7
	14,790.3	14,111.7	3,111.2	2,974.2	928.9	895.1
Other businesses	219.0	213.8	31.1	272.3	4.2	7.7
Corporate and unallocated	1,023.6	416.6	7,604.8	6,782.9	(4.8)	(3.9)
	16,032.9	14,742.1	10,747.1	10,029.4	928.3	898.9

<sup>(</sup>i) Segment assets consist of property, plant and equipment, investment properties, goodwill, other intangible assets, inventories, receivables and cash. Corporate and unallocated assets includes loan to related party, derivative financial instruments, pension assets and deposits (including deposits classified as cash).

<sup>(</sup>iii) Capital expenditure consists of additions to property, plant and equipment, intangible assets and investment properties.

d) Depreciation and amortisation	property, p	Depreciation on property, plant and equipment (Note 12)				sets (Note
	2020	2019	2020	2019		
	£m	£m	£m	£m		
Distribution network systems						
South West	61.7	59.5	3.5	2.4		
South Wales	42.8	40.0	0.6	0.4		
East Midlands	89.1	83.0	1.4	1.0		
West Midlands	83.3	74.8	1.2	0.9		
	276.9	257.3	6.7	4.7		
Other businesses	1.9	7.5	0.7	0.7		
	278.8	264.8	7.4	5.4		
Less: recapitalised to property, plant and equipment	(39.3)	(37.1)	-	-		
Charged to consolidated income statement	239.5	227.7	7.4	5.4		
4. Revenues		2020		2019		
		£m		£m		
Revenue from customer contracts		1,743.0		1,706.2		
Lease income		13.6		14.2		
		1,756.6		1,720.4		
The following table shows revenues from contracts with customers of	lisaggregated by custome	er class:				
-	·	2020		2019		
		£m		£m		
Licensed energy suppliers - DNO		1,614.1		1,598.0		
Other customers - DNO		82.9		64.3		
Other businesses customers		46.0		43.9		
		1,743.0		1,706.2		

<sup>(</sup>ii) Segment liabilities consist of deferred customer contributions and operating liabilities. Corporate and unallocated liabilities includes current taxation, corporate borrowings, derivative financial instruments and deferred taxation.

For the year ended 31 March 2020

# 4. Revenues (continued)

The licensed energy supplier revenue forms the majority of the external revenue of distribution network systems as disclosed in the Note 3 (a).

Network assets with a net book value of £12.9bn (2019: £12.2bn) are used to fulfil the contract with customers.

# 5. Operating costs

WPD Group operating costs can be applyed as follows:	2020	2019
WPD Group operating costs can be analysed as follows:	=	
	£m	£m
Employee benefit expense (Note 8)	152.1	144.6
Depreciation of property, plant and equipment	240.8	227.7
Property taxes	98.6	99.5
Other operating charges	193.3	209.1
	684.8	680.9
WPD Group operating profit is stated after charging/(crediting) the following		2010
	2020	2019
	£m	£m
Employee benefit expense (Note 8)	152.1	144.6
Depreciation of property, plant and equipment *	240.8	227.7
Amortisation of intangibles	7.4	5.4
Rent expense**:		
Plant, machinery and equipment		
I and and buildings	8.9	7.1
Land and buildings	8.9 0.5	7.1 0.6
Amortisation of customer contributions		

<sup>\*</sup> Depreciation of property, plant and equipment is stated net of depreciation capitalised of £39.3m (2019: £37.1m) in respect of equipment consumed during the construction of the electricity network. It also includes depreciation of right-of-use-assets amounting to £1.3m.

#### Services provided by the WPD Group's auditor

During the year the WPD Group obtained the following services from the Company's auditor and its associates:

	2020	2019
	£m	£m
Audit fees		
Annual audit of the Company and consolidated financial statements	0.1	0.1
Audit of subsidiary companies	0.7	0.5
Other audit related services	0.2	0.1
	1.0	0.7
Non-audit fees		
Audit related assurance services	0.1	0.3
	0.1	0.3
Total fees within operating costs	1.1	1.0

In addition, fees in respect of audit-related assurance services of £0.3m (2019: £0.3m) payable to Deloitte LLP were born by PPL Corp (the ultimate parent company) and so are excluded from this disclosure.

<sup>\*\*</sup> Rent expense pertains to short term and low value leases (refer to note 21).

<sup>\*\*\*</sup> Research and development costs above exclude expenditure on Low Carbon Network and Network Innovation Allowance projects which is capitalised together with associated funding received.

For the year ended 31 March 2020

6. Other operating income and expense	2020	2019
	£m	£m
Other operating income		
Net gain on disposal of property, plant and equipment	-	4.4
Increase in fair value of investment properties	0.2	1.5
Income from fixed asset investments	0.3	0.3
	0.5	6.2
Other operating expense		
Net loss on disposal of property, plant and equipment	(0.5)	-
Reduction in fair value of investment properties	(1.5)	(1.0)
Net other operating (expense)/income	(1.5)	5.2
7. Net finance costs	2020	2019
7. Net imance costs	£m	£m
Finance income		
Interest on bank deposits	1.4	1.0
Interest on loans to PPL affiliate (Note 33)	10.1	9.2
Total finance income	11.5	10.2
Finance costs		
Interest payable on bank loans and overdrafts	(2.8)	(3.6)
Interest payable on other loans	(298.2)	(285.0)
Interest payable on lease liabilities	(0.3)	-
Foreign exchange loss on US\$ denominated financial assets and liabilities	(32.7)	(43.8)
Transfers from the hedging reserve in relation to cash flow hedges	32.6	44.2
Less: interest capitalised	0.4	5.6
Total finance costs	(301.0)	(282.6)
Net finance costs	(289.5)	(272.4)

Interest in 2020 was capitalised at a rate of 1.7% (2019: 2.8%), based on the yield on the Group's borrowings.

# 8. Employee benefit expense

Employee benefit expense, including directors' remuneration, was as follows:

	2020	2019
	£m	£m
Wages and salaries	359.5	342.4
Social security costs	41.0	39.9
Pension costs	72.2	69.9
	472.7	452.2
Less: amounts capitalised as part of property, plant and equipment	(320.6)	(307.6)
Charged to the income statement	152.1	144.6

There are no personnel, other than the directors, who as key management have authority and responsibility for planning, directing and controlling the activities, directly or indirectly, of the WPD Group.

For the year ended 31 March 2020

#### 8. Employee benefit expense (continued)

The average number of employees during the financial year (including directors) analysed by activity was:

	2020	2019
	Number	Number
Electricity distribution	6,421	6,484
Other activities	153	159
	6,574	6,643

#### 9. Directors' emoluments

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

	Highest pai	d director	Tota	al
WPD Group	2020	2019	2020	2019
	€000	£000	£000	£000
The emoluments of the executive directors comprised:				
Base salary (note i)	423	465	1,266	1,520
Performance dependent bonus (note ii)	316	360	820	1,271
Pension compensation allowance (note iii)	217	212	374	363
Sub-total directors' remuneration	956	1,037	2,460	3,154
Long term incentive plan (note iv)	749	481	1,435	988
Fees to the independent non executive directors (note v)	-	-	100	100
Other (note vii)	-	-	-	9,400
	1,705	1,518	3,995	13,642

- (i) Base salary also includes benefits in kind.
- (ii) The amount of the annual bonus is based on WPD's financial performance, the reliability of the electricity network, and other factors.
- (iii) As a result of changes in tax applicable to UK pensions, two of the executive directors have resigned as active members of the Electricity Supply Pension Scheme ("ESPS" Note 27). Thus WPD no longer contributes for ongoing service to the ESPS in respect of these executive directors. Instead and subject to their service contract, WPD pays cash compensation to them individually equivalent to the value of WPD's contribution into the ESPS that would have been made had they remained active members (as determined by external actuaries). The remaining two executive directors are accruing ESPS service and WPD is contributing for ongoing service.
- (iv) Under a long term incentive plan, the executive directors were granted phantom stock options. The option price is set at the quoted share price of WPD's parent in the US, PPL Corporation, at the date the phantom options were granted. Options outstanding may be exercised during fixed periods and the gain is payable through the payroll. The values above include any payments made to the executive directors in respect of gains in value of phantom options exercised in the year. None of the executive directors was granted new options in either year; none of the executive directors exercised options (2019: two). In addition, the executive directors receive annually a grant of PPL Corporation shares which cannot generally be accessed for three years; the pay-out value of some of these shares is dependent on the achievement of certain performance criteria which may or may not be met and thus the final value may be considerably less. The value of the shares granted in the year is shown within this line.
- (v) The independent UK non executive directors are entitled to fees as determined by the appropriate Board. No emoluments are paid to US based non-executive directors, who are officers of PPL, in respect of their services as directors to the WPD Group.
- (vi) During the year, four executive directors (2019: five) were members of the defined benefit ESPS.
- (vii) Following the passing of WPD's previous Chief Executive Officer in November 2018, based on contractual obligations, an accrual of £9.4m was booked in the prior year with payment to the estate made in the current year in relation to death in service benefit.

For the year ended 31 March 2020

#### 10. Income tax expense

The major components of income tax expense are:	2020	2019
	£m	£m
Current tax		
Current tax expense (see below)	77.1	65.2
Adjustments in respect of prior years	(1.1)	(1.8)
Deferred tax (Note 26)		
Origination and reversal of temporary differences	56.7	66.3
Impact of tax rate change	68.4	(1.6)
Adjustments in respect of prior years	-	0.6
	201.1	128.7

The tax on the WPD Group's profit before tax differs from the theoretical amount that would arise using the standard rate of corporation tax in the UK of 19% (2019: 19%) as follows:

	2020 £m	2019 £m
Profit before income tax	749.7	733.2
Profit before income tax multiplied by standard rate of		
corporation tax in the UK of 19% (2019: 19%)	142.4	139.3
Effects of:		
Expenses not deductible and income not taxable for tax purposes	0.5	1.2
Group relief received at non-standard rates	(9.1)	(9.0)
Impact of tax rate change	68.4	(1.6)
Adjustments to tax charge in respect of prior years	(1.1)	(1.2)
Total taxation (continuing operations)	201.1	128.7

The total taxation expense as a percentage of profit before income tax gives an effective tax rate of 26.8% (2019: 17.6%) compared to the standard rate of 19% (2019: 19%) due to the effects of the items stated above. Expenses not deductible and income not taxable have been netted off as individually they are not material. Currently tax losses surrendered by PPL affiliates to the Group ("group relief") are not paid for and therefore the Group benefits by the tax value of these losses. The impact of the tax rate change in the current year is due to the reversal of the tax rate reduction that was expected to apply to the future years when the majority of deferred tax temporary differences are expected to reverse and in the prior year was due to the lower tax rate being used in the deferred tax calculations (see the change in corporation tax rate note below). Adjustments in respect of prior years mainly relate to the revised analysis of capital expenditure included in tax returns filed with HMRC and additional group relief received from PPL affiliates for no payment.

Tax relating to items (charged) or credited to other comprehensive income:	2020	2019
	£m	£m
Deferred tax:		
Revaluation of cash flow hedges	(1.4)	(2.5)
Re-measurement of pension liabilities	(66.7)	(25.4)
	(68.1)	(27.9)

#### Current tax expense

The current tax expense for the year is the aggregate of the amounts of UK corporation tax payable by each Group company on its profit for the year. The calculation of the amount of UK corporation tax payable is determined by tax legislation. The starting point for the calculation is the profit before tax shown in the income statement and adjustments required by the legislation are made to arrive at the profit chargeable to corporation tax. The calculation of the amount of corporation tax expected to be paid for the year is shown below. The actual amount payable will be determined following further detailed analysis at the time when the tax returns for the year for each Group company are filed with HMRC.

For the year ended 31 March 2020

# 10. Income tax expense (continued)

Current tax expense (continued)

Current tax expense (Continuea)	2020	2019	
	£m	£m	
	~III	2111	
Profit before income tax multiplied by standard rate of			
corporation tax in the UK of 19% (2019: 19%)	142.4	139.3	
Adjustments:			
Depreciation and amortisation (note i)	(13.2)	(22.8)	
Pensions (note ii)	(42.6)	(38.0)	
Other timing adjustments (note iii)	(0.6)	(1.6)	
Other adjustments (note iv)	0.2	(2.7)	
Corporation tax payable on profits before group relief	86.2	74.2	
Group relief (note v):			
Losses received from other group companies for free	(9.1)	(9.0)	
Corporation tax payable on profits after group relief	77.1	65.2	
The current tax charge on profits for the year is split as follows:			
Corporation tax payable to HM Revenue & Customs	77.1	65.2	
Group relief payable to other group companies	-	-	
	77.1	65.2	

- (i) Expenditure on tangible and intangible assets (net of related customer contributions) is initially recorded on the balance sheet and then depreciated or amortised over the useful economic lives of the assets. Tax deductions are not allowed for the depreciation or amortisation, except to the extent that the expenditure is regarded as maintaining or replacing part of an asset, and instead tax deductions are given for eligible expenditure at the rates prescribed by tax legislation ("capital allowances").
- (ii) The expense of providing pensions to employees is deductible from taxable profits at the time when contributions are paid into the pension schemes and not when the expense is charged to the income statement. As a proportion of the pension expense is capitalised (see Note 8), the deduction for contributions paid in the year is greater than the expense in the income statement.
- (iii) Adjustments are required for the timing of other deductions. These include interest capitalised (see Note 7) and employee benefit expense (see Note 8). A proportion of interest expense is included in tangible fixed asset additions, but the tax legislation provides for this expense to be deducted against profits for the year. Contrary to this, a deduction for employee benefit expense must be deferred until the year of payment if the payment is not made within nine months of the year end.
- (iv) Other adjustments are required for costs that are not deductible, such as legal fees relating to certain property transactions, and non-taxable income, such as dividends received from investments that have already paid tax on their income. In addition, the profit or loss on disposal of tangible fixed assets shown in the income statement is not taxable or deductible and is instead replaced with a gain or loss calculated in accordance with tax legislation.
- (v) The tax legislation allows a company that incurs a loss to surrender it to other companies within the same group to deduct from their taxable profits. Payment may be made up to the value of the loss without tax consequence.

#### Change in corporation tax rate

The Finance Act 2016 reduced the standard rate of corporation tax to 17% from 1 April 2020 and as this rate was enacted at 31 March 2019 it was used in the prior year to calculate the provision for deferred tax with respect to those temporary differences that were expected to reverse after the effective date. This rate reduction has been reversed by the Finance Bill 2020 and the rate will remain at 19% for the foreseeable future. This was substantively enacted on 17 March 2020 and the rate change has been reflected in the calculation of deferred tax for the current year.

For the year ended 31 March 2020

#### 11. Dividends

TI. Dividends	2020 £m	2019 £m
Equity dividends - 12.07 pence (2019: 18.11 pence) per £1 share	200.1	300.2

12. Property, plant and equipment						
			on-network		Vehicles	
		Distribution	land &	Fixtures &	& mobile	
	Generation	network		equipment	plant	Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 April 2018	0.5	13,958.3	154.9	275.8	127.1	14,516.6
Additions	-	828.4	5.6	37.1	11.3	882.4
Disposals and retirements	-	(1.7)	(3.8)	(23.7)	(5.2)	(34.4)
At 1 April 2019	0.5	14,785.0	156.7	289.2	133.2	15,364.6
Additions	_	863.6	8.4	31.0	13.3	916.3
Transfers	_	-	0.8	(0.8)	-	-
Disposals and retirements	-	(2.0)	-	(40.8)	(5.2)	(48.0)
At 31 March 2020	0.5	15,646.6	165.9	278.6	141.3	16,232.9
Accumulated depreciation						
At 1 April 2018	0.1	2,342.1	15.5	130.5	54.1	2,542.3
Depreciation charge for the year	-	210.7	2.3	38.3	13.5	264.8
Disposals and retirements	-	(1.7)	(0.3)	(23.7)	(4.5)	(30.2)
At 1 April 2019	0.1	2,551.1	17.5	145.1	63.1	2,776.9
Depreciation charge for the year	-	223.7	2.4	39.2	13.5	278.8
Disposals and retirements	-	(2.0)	-	(40.8)	(4.6)	(47.4)
At 31 March 2020	0.1	2,772.8	19.9	143.5	72.0	3,008.3
Net book value						
At 31 March 2020	0.4	12,873.8	146.0	135.1	69.3	13,224.6
At 31 March 2019	0.4	12,233.9	139.2	144.1	70.1	12,587.7
At 31 March 2018	0.4	11,616.2	139.4	145.3	73.0	11,974.3

Included in distribution network and vehicles & mobile plant at 31 March 2020 was an amount of £124.5m (2019: £86.5m) relating to expenditure on assets in the course of construction.

Included in additions are staff costs of £320.6m (2019: £307.6m), general overheads of £73.5m (2019: £73.4m) and interest of £0.4m (2019: £5.6m).

For the year ended 31 March 2020

## 13. Right-of-use asset

201 2119.11 02 400 40000	Land & buildings £m	Fibres £m	Radio sites £m	Total £m
At 1 April 2019 - transition to IFRS 16	7.5	2.9	0.4	10.8
Additions	0.4	0.1	-	0.5
Depreciation	(0.5)	(0.7)	(0.1)	(1.3)
At 31 March 2020	7.4	2.3	0.3	10.0

Lease liabilities and the corresponding right-of-use-assets have been recognised on the balance sheet due to transition to the new IFRS 16 "Leases" effective for the Group from 1 April 2019.

#### 14. Investment property

	Retail	Office	Industrial	Total
	£m	£m	£m	£m
Fair value				
At 1 April 2018	22.5	7.1	5.4	35.0
Valuation gains	-	0.7	0.8	1.5
Valuation losses	(0.4)	(0.3)	(0.3)	(1.0)
Disposals	(0.2)	(2.2)	(0.6)	(3.0)
At 1 April 2019	21.9	5.3	5.3	32.5
Valuation gains	0.1	-	0.1	0.2
Valuation losses	(1.0)	(0.2)	(0.3)	(1.5)
Transfers to property, plant and equipment	-	-	(0.8)	(0.8)
Disposals	(0.3)	-	-	(0.3)
At 31 March 2020	20.7	5.1	4.3	30.1

The fair value of investment property is based mostly on valuations by independent valuers (Alder King, Jones Lang Lasalle, Hartnell Taylor Cook, PNB Paribas), with the remaining valuations carried out by a qualified surveyor who is an employee of the WPD Group. All valuers are either members of the Royal Institution of Chartered Surveyors ("MRICS") or Fellows of the Royal Institution of Chartered Surveyors ("FRICS"). It is the WPD Group's policy that all properties are valued independently at least once every five years, with more frequent independent valuations carried out for higher value properties. The valuers all have recent experience in the location and category of the investment property being valued. The properties were valued on the basis of open market value in accordance with the Appraisal and Valuation Manual of the Royal Institution of Chartered Surveyors.

The WPD Group's current use of the properties as investment properties is considered to be their highest and best use.

The amounts recognised in the income statement for rental income from investment property are £2.6m (2019: £2.6m).

Investment properties are let on either full repair and insuring leases, under which all outgoings are the responsibility of the lessee, or under tenancies, where costs are recovered through a service charge levied on tenants during the period of occupation. This service charge amounted to £0.5m (2019: £0.5m) for which a similar amount is included within operating costs.

In determining the appropriate classes of investment property the Group has considered the nature, characteristics and risks associated with its properties. As a consequence the Group has identified the following classes of assets:

- Retail representing a single investment in a supermarket store in Cwmbran, South Wales, occupied by J Sainsbury.
- Other retail representing a portfolio of other retail properties across Wales and the South West of England.
- Office representing a portfolio of office buildings across WPD's region.
- Industrial representing a portfolio of industrial and storage facilities across WPD's region.

The tables below show details for the larger properties. Within other assets, recorded at £4.6m (2019: £6.0m), are a further 24 (2019: 44) investment properties with an average value of £192,000 per property (2019: £136,000), valued by the WPD Group's internal qualified surveyor.

For the year ended 31 March 2020

### 14. Investment property (continued)

All of the assets are valued on an Income Capitalisation methodology whereby rents receivable are divided by an appropriate yield. The valuations take into account existing tenancies and where necessary make appropriate assumptions regarding vacancies arising at future rent renewal dates.

The outbreak of the COVID-19 pandemic has led to global economic disruption and volatility in all business sectors including real estate. The future impact of COVID-19 on the real estate market is currently unknown but the continued spread of the virus and efforts to contain the virus such as quarantines and extended closures of businesses can adversely impact the fair values of investment properties. Consequently, our valuers have reported fair values on the basis of "material valuation uncertainty" as per the Royal Institution of Chartered Surveyors ("RICS") Red Book Global. Material valuation uncertainty does not imply that the valuation cannot be relied upon but indicates that due to extraordinary circumstances less certainty could be attached to the valuation. Management will continue to closely monitor the implications of COVID-19 on the fair values of investment properties.

All of the valuations fall within Level 3 of the fair value hierarchy (see Note 24). The table below provides details by class of property of the fair value ascribed to each class of asset, an indication of the key inputs used in deriving the valuation, together with other key features which inform the valuation process. In light of the immaterial nature of the other assets below to the financial statements as a whole, the directors have elected not to provide the equivalent detailed information in respect of these valuations.

The valuations are sensitive to movements in key variables, notably the yields applied to valuations based on income capitalisation which can change due to general market conditions and also an assessment of the quality of the underlying tenant. Broadly, a 0.5% increase/decrease in an assumed yield of 5% will result in a 10% decrease/increase in the value of a property, whilst a 0.5% increase/decrease in an assumed yield of 10% will result in a 5% decrease/increase in the value of a property.

Unobservable and observable inputs used in determination of fair values

Other key information

Class of property	Carrying amount/Fair value 2020 £m	Valuation technique	Input	Range (weighted average) 2020		Range 2020
Retail	16.5	Income	> Length of leases in place	. Qv	> Age of building	26y
Level 3		capitalisation	(in years)	•	> Remaining useful life of	20+
			> Yield	5.2%	building	
			> Passing rent (per sqm p.a.)	£201.4	> Square metres	5,308
			> Long term vacancy rate	0%		
Other retail	2.9	Income	> Net rent (per sqm p.a.)	£93 - £230	> Age of building	50+
Level 3		capitalisation	> Net lent (per squi p.a.)	(£160)	> Remaining useful life of	20+
			> Length of leases in place	0y - 5y	building	201
			(in years)	(1.9y)	> Square metres	2,175
			> Yield	7.3% - 8.0%	> Actual vacancy rate	0%
			> Long term vacancy rate	0%		
Office	4.0	Income	> Net rent (per sqm p.a.)	£50 - £165	> Age of building	22y - 37y
Level 3		capitalisation	> Net tent (per squi p.a.)	(£86)	> Remaining useful life of	20+
			> Length of leases in place	0y - 9y	building	20+
			(in years)	(6.7y)	> Square metres	6,619
			> Yield	1% - 7%	> Actual vacancy rate	0% - 97%
			> Long term vacancy rate	0% - 97% (84%	)	
Industrial	2.1	Income	> Net rent (per sqm p.a.)	£36- £76	> Age of building	64y
Level 3		capitalisation	> Net tent (per squi p.a.)	(£63)	> Remaining useful life of	20+
			> Length of leases in place	2y - 22y	building	20+
			(in years)	(15y)	> Square metres	3,106
			> Yield	10%	> Actual vacancy rate	0%
			> Long term vacancy rate	0%		
Total	25.5					
Other assets	4.6					

Total fair value 30.1

For the year ended 31 March 2020

# 14. Investment property (continued)

Unobservable and observable inputs used in determination of fair values

Other key information

Class of property	Carrying amount/Fair value 2019 £m	Valuation technique	Input	Range (weighted average) 2019		Range 2019
Retail Level 3	16.5	Income capitalisation	> Length of leases in place (in years)	<sup>2</sup> 10y	> Age of building > Remaining useful life of	25y
		1	> Yield	5.2%	building	20+
			> Passing rent (per sqm p.a.)	£201.4	> Square metres	5,308
			> Long term vacancy rate	0%	•	ŕ
Other retail	3.6	Income		£93 - £204	> Age of building	50+
Level 3		capitalisation	> Net rent (per sqm p.a.)	(£155)	> Remaining useful life of	20+
		_	> Length of leases in place	2y - 6y	building	20+
			(in years)	(3.4y)	> Square metres	2,175
			> Yield	7.3% - 8.0%	> Actual vacancy rate	0%
			> Long term vacancy rate	0%		
Office	4.3	Income	> Net rent (per sqm p.a.)	£50 - £165	> Age of building	21y - 36y
Level 3		capitalisation	> Net tent (per squi p.a.)	(£86)	> Remaining useful life of	20+
			> Length of leases in place	1y - 10y	building	20+
			(in years)	(8y)	> Square metres	6,619
			> Yield	1% - 7%	> Actual vacancy rate	0% - 97%
			> Long term vacancy rate	0% - 97% (84%	•	
Industrial	2.1	Income	> Net rent (per sqm p.a.)	£36- £76	> Age of building	63y
Level 3		capitalisation	> Net tent (per squi p.a.)	(£63)	> Remaining useful life of	25y
			> Length of leases in place	3y - 23y	building	23 y
			(in years)	(16y)	> Square metres	3,106
			> Yield	10%	> Actual vacancy rate	0%
			> Long term vacancy rate	0%		
Total	26.5					
Other assets	6.0					
Total fair val	ue 32.5					

For the year ended 31 March 2020

15. Intangible assets	Goodwill	Computer software	Customer contracts	Total
Cost:	£m	£m	£m	£m
At 1 April 2018	1,574.5	36.6	6.2	1,617.3
Additions	-	16.5	-	16.5
At 1 April 2019	1,574.5	53.1	6.2	1,633.8
Additions	-	12.0	-	12.0
Transfers from property, plant and equipment	-	0.8	-	0.8
At 31 March 2020	1,574.5	65.9	6.2	1,646.6
Aggregate amortisation and impairment:				
At 1 April 2018	320.4	10.9	4.2	335.5
Charge for the year	-	4.8	0.6	5.4
At 1 April 2019	320.4	15.7	4.8	340.9
Charge for the year	-	6.7	0.7	7.4
At 31 March 2020	320.4	22.4	5.5	348.3
Carrying amount At 31 March 2020	1,254.1	43.5	0.7	1,298.3
At 31 March 2019	1,254.1	37.4	1.4	1,292.9
At 31 March 2018	1,254.1	25.7	2.0	1,281.8

Goodwill acquired through business combinations has been allocated for impairment testing purposes to three cash-generating units ("CGUs"), East Midlands, West Midlands, and South Wales, which are also operating segments. These represent the lowest level within the WPD Group at which goodwill is monitored for internal management purposes. At 31 March 2014, an impairment loss of £186.2m and £62.2m was recognised in East Midlands and West Midlands, respectively. A further impairment loss of £72.0m was recognised at 31 March 2015 in West Midlands.

Carrying amount of goodwill allocated to cash-generating units ("CGUs")	2020 £m	2019 £m
East Midlands	518.8	518.8
West Midlands	614.4	614.4
South Wales	120.9	120.9
Carrying amount of goodwill	1,254.1	1,254.1

In assessing whether goodwill has been impaired, the carrying amount of the CGU (including goodwill) is compared with the recoverable amount of the CGU. The recoverable amount is the higher of fair value less costs to dispose and value in use.

The WPD Group calculates the recoverable amount as the higher of the value in use using a discounted cash flow model and fair value less cost to dispose. The key assumptions for the value in use calculations are those regarding the discount rate, expected cash flows arising from revenues, direct costs, and capital expenditure during the forecast period, and the multiple applied to the Regulatory Asset Value ("RAV") at the end of the period to determine the terminal value.

CGU cash flows are derived from the corporate business plan approved by management. In determining the value in use, cash flows for a period of eight years have been discounted and aggregated with a terminal value, which is calculated by applying a multiple to the RAV at the end of the period. A period of greater than five years has been used as the period is covered by the corporate business plan and more accurately reflects the timing of cash outflows associated with major capital replacement cycles and their subsequent recovery under electricity distribution regulation. This period covers the remainder of RIIO-ED1 where the business plan has been agreed with Ofgem and a forecast for RIIO-ED2, which is yet to be agreed with Ofgem.

For the year ended 31 March 2020

### 15. Intangible assets (continued)

The pre-tax future cash flows are discounted using a pre-tax rate discount rate of 5.00% (2019: 4.84%). WPD's post-tax weighted average cost of capital ("WACC)" is estimated and converted to a pre-tax discount rate using an iterative calculation approach in the value in use methodology. During the year, WPD's post-tax WACC, used to calculate the pre-tax discount rate, has been increased by an alpha premium of 1% to account for the current uncertainty in the cash flows in relation to Ofgem's final determinations for RIIO-ED2.

The key assumptions during the electricity price control period from 1 April 2015 to 31 March 2023 ("RIIO-ED1") are based on revenues allowed and cost of capital assumptions agreed at the most recent electricity price control review, together with management's expectation of the related cost and capital expenditure requirements during that period. The view for the remainder of RIIO-ED1 has been updated to reflect our current performance in the price control.

Assumptions beyond this period are based on the approved budget and the Board's expectation of the outcome of future price control review i.e. RIIO-ED2. Key RIIO-ED2 assumptions in relation to cost of equity allowances, incentive revenues and totex have been determined by taking into consideration current information such as RIIO-ED2 framework consultations, existing determinations by Ofgem, as well as our performance in the current price control, the latest published policy intent from Ofgem and the Government and various other industry information. Forecast incentive revenue represents management's best estimate at this point in time as Ofgem has yet to release guidance on the potential incentive package. In the current year our forecast for RIIO-ED2 and relevant assumptions has been updated to incorporate the Government's and Ofgem's latest views on net-zero carbon targets, electric vehicle rollout and the DSO strategy. Due to the transitioning of DNO to DSO, reinforcement cash flows in the business plan have been updated to reflect the forecasted spend on future network and flexible energy projects. The key assumptions in respect of RIIO-ED2 cash flows will continue to evolve as the price control approaches and Ofgem produces clearer guidance; as such we have modelled some reasonable possible changes to these key assumptions below.

The impact of the global pandemic, COVID-19, has been taken into consideration in estimating the future cash flows of each CGU. Following the announcement of restrictions, the capital programme was disrupted in the short term and the work focused on essential and critical activities whilst continuing to provide a safe, secure and reliable supply of energy to our customers. As at July 2020, the Group has resumed operations in relation to non-safety critical capital programmes, subject to appropriate safety measures. Revenues have been impacted temporarily due to reduced load demand from industrial and commercial customers, slightly offset by an increased demand from domestic customers as a direct result of businesses and the public adhering to Government restrictions during March to July 2020. Any impact on revenue is largely a timing issue due to the regulatory regime that provides for recovery of allowed revenue under a price control period. This impact on the timing of net cash flows has been taken into consideration in determining the estimated future cash flows of the CGUs.

Due to timing of goodwill impairment test, a forecasted RAV for 31 March 2020 is used in the business plan and is £2,526.9m (2019: £2,459.9m), £2,541.1m (2019: £2,464.2m) and £1,190.9m (2019: 1,134.0m) for East Midlands, West Midlands and South Wales, respectively. The terminal value multiple applied to the RAV at the end of the cash flow period, i.e. 31 March 2028, is 35% (2019: 25%). The terminal value multiple has been increased in order to align with recent relevant market transactions. Management believes the increase in the multiple during the year is also appropriate in light of the UK Government's increased environmental focus on climate change. During the year the Government legislated the move towards a net-zero carbon economy by 2050 which will drive a need for significant reinforcement of electricity networks to facilitate renewable generation. Decarbonisation of transport and heat are two key areas of focus and are likely to be a significant part of the electrification solution to achieve the Government's strategy. Thus DNOs have a significant role to play in delivering the Government's targets in the foreseeable future.

The pre-tax cash flows reflect an implied growth of 2.9%-3.8% (2019: 3.1%-4.1%). The implied growth rate from management's discounted cash flow model and multiple applied to the terminal RAV value, slightly exceeds the long term forecasted RPI for the UK. Management support this long term growth rate as the RIIO regulatory regime incentivises the Company to realise real growth above RPI when it reaches target performance measures. The Group has a historic track record of achieving such performance targets and forecasts a consistent level of performance in the future.

At 31 March 2020, the East Midlands, West Midlands, and South Wales recoverable amounts exceeded their carrying amounts by £156.0m, £141.1m, and £89.4m (2019: £43.3m, £80.1m and £46.9m), respectively. The increase in the headroom during the year is due to the increase in the terminal value multiple from 25% to 35%, which is partially offset by increase in the discount rate during the year due to an additional alpha premium being incorporated within the WPD Group's WACC calculation.

In assessing the carrying value of goodwill, the cash flows have been sensitised to various reasonable possible changes in assumptions and the analysis reflects sufficient headroom. The key reasonable possible changes and sensitivities to assumptions are presented below:

For the year ended 31 March 2020

### 15. Intangible assets (continued)

Reasonable possible changes in key assumptions:	East Midlands Rec	West Midlands duction in recov	South Wales verable amounts	Total
	£m	£m	£m	£m
0.85% increase in the pre-tax discount rate from 5.0% to 5.85%	(226.0)	(223.1)	(106.4)	(555.5)
5.0% decrease in terminal value multiple on the RAV from $35%$ to $30%$	(124.7)	(119.2)	(59.6)	(303.5)
1.0% decline in RIIO-ED2 cost of equity allowance	(52.4)	(51.5)	(24.9)	(128.8)
1.0% decline in RIIO-ED2 incentive revenue on return on regulatory equity basis ("RoRE")	(30.6)	(30.6)	(15.3)	(76.5)
1.0% decline in RIIO-ED2 cost of equity allowance and 1.0% decline in incentive revenue on RoRE basis	(83.0)	(82.1)	(40.2)	(205.3)

A reasonable possible change in discount rate on its own will lead to an impairment. As would a combination of reasonable possible changes to terminal RAV multiple and RIIO-ED2 assumptions.

The discounted pre-tax cash flows of East Midlands, West Midlands and South Wales reflect an implied premium on current RAV of 55.5%, 54.9% and 52.3%, respectively. Sensitivity analysis to the current implied premium to RAV is as follows:

	East	West	South	
	Midlands	Midlands	Wales	Total
	(Decrea	se) / increase i	n recoverable am	ounts
	£m	£m	£m	£m
Implied premium to current RAV at 45%	(264.4)	(251.7)	(86.7)	(602.8)
Implied premium to current RAV at 50%	(138.1)	(124.6)	(27.1)	(289.8)
Change in assumption required to eliminate all headroom:				
Increase in the pre-tax discount rate	by 0.58%	by 0.53%	by 0.71%	
	to 5.58%	to 5.53%	to 5.71%	
Decrease in the terminal value multiple	by 6%	by 6%	by 8%	
	to 129%	to 129%	to 127%	

A decline of 3.0%, 2.7% and 3.6% in the assumed cost of equity allowance on RIIO-ED2 for the East Midlands, West Midlands and South Wales, respectively, would remove all headroom.

The elimination of assumed RIIO-ED2 incentive revenues, would not result in an impairment.

## 16. Investments

(a) Investment at amortised cost	2020	2019
	£m	£m
Investment in PPL affiliate debt	161.9	154.9

In February 2011, the WPD Group purchased \$200m nominal at a premium price of \$21m from PMDC Chile of the \$400m 2018 6.42% USD denominated Eurobond issued by PPL UK Resources Limited. During the prior year the maturity date was extended to 2021.

The expected credit loss on investments at amortised cost as at 31 March is as follows:	2020 £m	2019 £m
At 1 April - IAS 39	-	-
Amount restated through opening retained earnings	-	0.1
Restated at 1 April - IFRS 9	0.1	0.1
Provision for impairment	<u>-</u>	
At 31 March	0.1	0.1

For the year ended 31 March 2020

#### 16. Investments (continued)

### (b) Details of WPD Group undertakings

A list of investments in subsidiaries, including the name, country of incorporation, and proportion of ownership interest, is given in Note 4 to the Company's separate financial statements.

### 17. Inventories

	2020	2019
	£m	£m
Raw materials	37.5	23.1
Work in progress	1.0	1.1
	38.5	24.2

Inventory as at 31 March 2020 includes critical stock ordered in bulk in response to the risk of any potential inventory shortage due to Brexit.

The cost of inventories recognised as an expense during the year was £8.8m (2019: £10.9m). The cost of inventories recognised as an expense includes £0.5m (2019: £0.9m) in respect of write downs of inventory to net realisable value and has been reduced by £0.4m (2019: £0.2m) in respect of reversal of such write downs.

18. Trade and other receivables	2020	2019
	£m	£m
Current receivables		
Trade receivables	275.9	261.2
Other receivables	4.7	2.8
Accrued income	6.2	9.9
Prepayments	21.0	18.9
Total current receivables	307.8	292.8
Non-current receivables		
Other receivables	1.0	5.0
Prepayments	1.0	1.0
Total non-current receivables	2.0	6.0
Total trade and other receivables	309.8	298.8

The carrying amount of trade and other receivables and loan to related party is considered to approximate their fair value.

Other receivables relate primarily to insurance claims and the non-current balances that are expected to be recovered over the next three years.

As at 31 March 2020, trade receivables and accrued income at a nominal value of £2.9m (2019: £3.3m) were impaired and fully provided for. Movements in the provision for impairment were as follows.

	2020	2019
	£m	£m
At 1 April - IAS 39	-	1.7
Amount restated through opening retained earnings - IFRS 9	<u>-</u>	0.4
Restated 1 April - IFRS 9	3.3	2.1
Provision for impairment	1.9	8.1
Amounts written off as uncollectable	(0.9)	(1.3)
Amounts recovered during the year	(1.3)	(5.6)
At 31 March	3.0	3.3

The WPD Group considers 100% of its credit risk to be with counterparties in related industries. The maximum credit risk exposure is represented by the carrying value as at the balance sheet date.

For the year ended 31 March 2020

#### 18. Trade and other receivables (continued)

As at 31 March, the aged analysis of trade receivables is as follows:

	N	Neither past due		Past due but not impaired			
	Total	nor impaired	<30 days	30-60 days	60-90 days	90-120 days	>120 days
	£m	£m	£m	£m	£m	£m	£m
2020	275.9	260.6	5.8	1.5	0.6	0.6	6.8
2019	261.2	252.1	3.3	1.9	2.1	1.4	0.4

Trade receivables that are neither past due nor impaired relate largely to charges made to electricity suppliers for the use of WPD's distribution network. Credit risk management for these receivables is performed in accordance with industry standards as set out by Ofgem and governed by the credit rules within the DCUSA.

The impact of COVID-19 on ECL has been assessed and is not material. Ofgem regulations allow for full recoverability of credit losses on DUoS debtors, provided certain credit management protocols are performed in accordance with industry standards as governed by the DCUSA, thus minimising any potential credit risk to the Group. Further, since mid-March 2020 no material slowdown in receipts has been noted.

In order to minimise exposure to debt, the DCUSA requires WPD to monitor electricity suppliers' (WPD's customers) indebtedness ratios daily to ensure it does not exceed 85%. The indebtedness ratio is defined as 'Value at Risk/Credit Limit' where 'Value at Risk' is the suppliers' current outstanding invoices plus a 15 day estimate of unbilled amounts and 'Credit Limit' is calculated by reference to WPD's RAV, the suppliers' credit rating from an approved credit referencing agency, and the suppliers' payment performance history.

Where necessary, suppliers can ensure they are within the 85% indebtedness threshold by providing collateral to increase their 'Credit Limit'. This can be in the form of a letter of credit or equivalent bank guarantee, an escrow account deposit, a cash deposit, or any other form of collateral agreed between WPD and the supplier. At 31 March 2020, the WPD Group held collateral in relation to trade receivables in the form of cash £2.2m (2019: £2.2m), letters of credit £53.3m (2019: £57.0m), and parent company guarantees £61.3m (2019: £54.5m). Letters of credit have a rating of Moody's A2/S&P A or greater. The maximum amounts for parent company guarantees are based on their credit ratings as per the DCUSA regulations.

19. Cash at bank and in hand	2020 £m	2019 £m
	oviii	2111
Cash at bank	64.4	52.8
Short-term bank deposits	136.6	89.9
Cash at bank and in hand	201.0	142.7

The fair value of cash at bank is considered to approximate its carrying amount. Short term deposits are measured at fair value through profit and loss ("FVTPL"). Cash at bank earns interest at floating rates based on short-term bank deposit rates. Short-term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the WPD Group, and earn interest at the respective short-term deposit rates.

At 31 March 2020, the WPD Group had available £794.0m (2019: £812.8m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met. All facilities incur commitment fees at market rates. At 31 March 2020, it also had available undrawn uncommitted facilities of £96.5m (2019: £96.5m).

Included in cash and short-term bank deposits are restricted amounts totalling £13.2m (2019: £14.2m) which are not readily available for the general purposes of the WPD Group. The restrictions relate largely to minimum cash balances that are required to be maintained for insurance purposes and cash balances that can only be used for low carbon network fund projects.

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise the following at 31 March:

	2020	2019
·	£m	£m
Cash at bank and in hand (from above)	201.0	142.7
Bank overdrafts (Note 22)	(13.5)	(19.5)
Cash at bank and in hand in the cash flow statement	187.5	123.2

Bank overdrafts comprise principally unpresented cheques at the year end.

For the year ended 31 March 2020

### 20. Trade and other payables

2020	2019
£m	£m
44.2	59.0
65.4	60.0
141.5	134.7
13.1	15.0
46.1	45.3
291.4	266.3
601.7	580.3
2,588.7	2,481.6
3,190.4	3,061.9
	£m  44.2 65.4 141.5 13.1 46.1 291.4  601.7

Trade and other payables comprise amounts outstanding for trade purchases and ongoing costs. Deferred contributions are those amounts received from customers in respect of new connections to the network. The carrying amount of trade and other payables is considered to approximate their fair value.

### 21. Lease liabilities

	<u>£m</u>
At 1 April 2019 - transition to IFRS 16	10.8
Additions	0.5
Payments during the year	(1.5)
Interest expense	0.3
At 31 March 2020	10.1
of which	
Current	1.5
Non-current	8.6

The WPD Group leases various properties under non-cancellable operating lease arrangements. In addition to this, WPD leases in rights to capacity on third party fibre optic networks, and space and equipment at third party telecommunication sites, under non-cancellable lease arrangements, in order to extend its core fibre network for its point to point transmission services. The leases have various terms, escalation clauses and renewable rights. Lease terms and rentals to be paid during the lease term are defined within the agreement. In some cases, lease rentals may be subject to a rent review on dates specified within the agreement at the then prevailing market rate.

Short term leases and low value leases are excluded from recognition on the balance sheet. The amount of expense charged to rent expense pertaining to short term leases amounts to £5.2m and pertaining to low value leases amounts to £0.7m.

Lease liabilities and the corresponding right-of-use-assets have been recognised on the balance sheet due to the transition to the new IFRS 16 "Leases" effective for the Group from 1 April 2019.

## 22. Loans and other borrowings

	2020	2019
	£m	£m
Current		_
Bank overdrafts (Note 19)	13.5	19.5
Syndicated credit facilities (i)	261.1	244.0
9.250% GB£150m bonds due 2020	151.6	
	426.2	263.5

<sup>(</sup>i) The syndicated credit facilities contain financial covenants to maintain an interest coverage ratio of not less than 3.0 times consolidated earnings before income taxes, depreciation and amortisation and total net debt not in excess of 85% of RAV, calculated in accordance with the credit facility. At 31 March 2020, £100.0m (2019: £90.6m) of syndicated credit facilities were denominated in Sterling and £161.0m (2019: £153.4m) were denominated in US dollars.

For the year ended 31 March 2020

## 22. Loans and other borrowings (continued)

22. Zoulo una outer sorro mago (continuo)	2020	2019
	£m	£m
Non-current		
5.875% GB£250m bonds due 2027 (iv)	248.9	248.7
5.75% GB£200m bonds due 2040 (iv)	197.6	197.5
2.375% GB£250m bonds due 2029	247.0	246.7
9.250% GB£150m bonds due 2020 (iv)	-	154.0
4.804% GB£225m bonds due 2037 (i) (iv)	220.9	220.7
5.75% GB£200m bonds due 2040 (iv)	197.6	197.5
6.25% GB£250m bonds due 2040 (iv)	257.4	257.7
5.25% GB£700m bonds due 2023 (iv)	700.8	701.1
6.00% GB£250m bonds due 2025 (iv)	252.5	253.0
5.75% GB£800m bonds due 2032 (iv)	791.9	791.2
3.875% GB£400m bonds due 2024 (iv)	397.5	396.9
3.625% GB£500m bonds due 2023	497.6	496.9
5.375% US\$500m bonds due 2021	402.3	383.0
7.375% US\$202m bonds due 2028	156.1	147.6
3.5% GB£350m bonds due 2026	345.7	345.1
1.75% GB£250m bonds due 2031	245.5	-
£50m 5 year term loan	49.7	-
1.541% + RPI GB£105m index linked bonds 2053 (ii) (iii)	152.4	148.4
1.541% + RPI GB£120m index linked bonds 2056 (ii) (iii)	174.1	169.6
0.010% + RPI GB£50m index linked bonds 2029 (iii)	56.6	55.4
0.010% + RPI GB£30m index linked bonds 2036 (iii)	32.5	31.7
2.671% + RPI GB£140m (2016: £100m) index linked bonds 2043 (iii)	207.1	203.9
1.676% + RPI GB£105m index linked bonds 2052 (iii)	136.2	133.4
0.4975% + RPI GB£100m index linked bonds 2026 (iii)	111.3	108.4
1.25% + RPI GB£30m index linked bonds due 2028 (iii)	31.8	31.1
	6,111.0	5,919.5
Total loans and other borrowings	6,537.2	6,183.0

- (i) May be redeemed, in total but not in part, on 21 December 2026, at the greater of the principal value or a value determined by reference to the gross redemption yield on a nominated UK Government bond.
- (ii) May be redeemed, in total by series, on 1 December 2026, at the greater of the adjusted principal value and a make-whole value determined by reference to the gross real yield on a nominated UK government bond.
- (iii) The principal amount of the notes is adjusted based on changes in a specified index, as detailed in the terms of the related indentures. The adjustment to the principal amounts in 2020 was an increase of approximately £22.3m resulting from inflation.
- (iv) May be put by the holders to the issuer for redemption if the long-term credit ratings assigned to the notes are withdrawn by any of the rating agencies (Moody's or S&P) or reduced to a non-investment grade rating of Ba1 or BB+ in connection with a restructuring event which includes the loss of, or a material adverse change to, the distribution licences under which the issuer operates.

None of the outstanding debt securities noted above has sinking fund requirements.

The carrying amounts of the WPD Group's borrowings are denominated in the following currencies:

, ,	2020	2019
	£m	£m
UK pound	5,817.8	5,499.0
US dollar	719.4	684.0
	6,537.2	6,183.0

For the year ended 31 March 2020

## 23. Reconciliation of liabilities arising from financing activities

25. Reconcination of natificies arising from financing activities	2020	2019
	£m	£m
Borrowings	6,537.2	6,183.0
Lease liabilities	10.1	-
Derivatives in hedging relationship	(163.1)	(102.8)
Gross debt net of related derivatives	6,384.2	6,080.2
Change in liabilities arising from financing activities		
	2020	2019
	£m	£m
Cash flow per financing activity section of cash flow statement		
Net increase/(decrease) in short term borrowings	3.0	(194.8)
Proceeds from long term borrowings net of issue costs	295.0	375.4
Payment of lease liabilities	(1.5)	-
Change in liabilities arising from financing activities	296.5	180.6
Non-cash adjustments		
Net increase in derivatives	(60.3)	(53.2)
Foreign exchange loss on borrowings	34.8	48.9
Net increase in borrowings due to indexation	22.3	20.0
Amortisation of premiums, discounts and issue costs	(0.9)	(1.6)
Leases acquired during the year	11.3	-
Interest expense on lease	0.3	-
Movement in gross debt net of related derivatives in the year	304.0	194.7
Gross debt net of related derivatives at beginning of year	6,080.2	5,885.5
Gross debt net of related derivatives at end of year	6,384.2	6,080.2

### 24. Financial instruments

Financial risk management objectives and policies

The WPD Group's principal financial liabilities, other than derivatives, comprise bank loans and overdrafts, bonds and trade payables. The main purpose of these financial liabilities is to raise finance for the WPD Group's operations. The WPD Group has various financial assets such as trade receivables and cash and short-term deposits, which arise directly from its operations.

The WPD Group also enters into derivative transactions, principally interest rate and cross currency swaps. The purpose is to manage the interest rate and currency risks arising from the WPD Group's operations and its sources of finance.

It is, and has been throughout 2020 and 2019, the WPD Group's policy that no speculative trading in financial instruments shall be undertaken.

The main risks arising from the WPD Group's financial instruments are fair value interest rate risk, liquidity risk, foreign currency risk and credit risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

## Market risk

Market risk is the risk that movements in market rates, including foreign exchange rates, interest rates and inflation will affect the WPD Group's profit. The management of market risk is undertaken with risk limits approved by the Board.

For the year ended 31 March 2020

### 24. Financial instruments (continued)

#### Interest rate risk

The WPD Group has issued debt to finance its operations, which exposes it to interest rate risk. Borrowings issued at variable rates expose the WPD Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the WPD Group to fair value interest rate risk. The WPD Group's interest rate risk management policy includes achieving the lowest possible cost of debt financing, while managing volatility of interest rates, applying a prudent mix of fixed and floating debt, either directly or through the use of derivative financial instruments affecting a shift in interest rate exposures between fixed and floating, and also matching debt service requirements to projected cash flows. The WPD Group's policy stipulates that a maximum of 25% of WPD Group borrowings be subject to variable rates of interest.

The WPD Group may use forward-starting interest rate swaps to minimise exposure to cash flow interest rate risk for future forecast issuance of debt.

The net exposure to interest rates at the balance sheet date can be summarised thus:

1	2020	2019
	Carrying	Carrying
Interest bearing/earning assets and liabilities:	amount	amount
	£m	£m
Fixed	5,040.1	4,782.6
Floating	73.6	120.8
Index-linked	902.0	881.9
	6,015.7	5,785.3
	2020	2019
	Carrying	Carrying
Represented by:	amount	amount
	£m	£m
Cash and cash equivalents	(201.0)	(142.7)
Investment in parent company debt	(161.9)	(154.9)
Derivative financial assets/liabilities	(158.6)	(100.1)
Loans and borrowings	6,537.2	6,183.0
	6,015.7	5,785.3

#### Interest rate sensitivity

The impact of a change in interest rates is dependent on the specific details of the financial asset or liability in question. Changes in fixed rate financial assets and liabilities, which account for the majority of loans and borrowings, are not measured at fair value through the income statement. In addition to this, changes to fixed-to-fixed hedging instruments which are recorded under cash flow hedge accounting also do not impact the income statement. Changes in variable rate instruments are recorded through the income statement. The exposure measured is therefore based on variable rate debt.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, on the WPD Group's profit before tax (through the impact on floating rate borrowings). There is no impact on the WPD Group's equity.

The sensitivity analysis excludes all non-derivative fixed rate financial instruments carried at amortised cost but includes all non-derivative floating rate financial instruments.

Currency derivatives have not been included in the sensitivity analysis below as they are not considered to be exposed to interest rate risk.

All sensitivity analysis has been prepared on the basis of the proportion of fixed to floating instruments being consistent as at the balance sheet date. The sensitivity analysis is indicative only and it should be noted that the WPD Group's exposure to such market rate changes is continually changing. The calculation is based on linear extrapolations of rate changes which may not reflect the actual result which would impact upon the WPD Group.

For the year ended 31 March 2020

### 24. Financial instruments (continued)

Interest rate sensitivity (continued)

	2020		2019	
	Income		Income	
	statement		statement	
	(before tax)	Equity	(before tax)	Equity
	+/- <b>£m</b>	+/ <b>- £m</b>	+/- £m	+/- £m
Interest Rate +/- 100bp	0.7	-	(1.2)	-

### Inflation risk

The WPD Group's index-linked borrowings and interest liabilities are exposed to a risk of change in the carrying value due to changes in the UK RPI. This form of liability is a good match to the WPD Group's regulated assets ("RAV"), which are also linked to RPI due to the price setting mechanism imposed by the regulator, and also the price cap is linked to RPI. By matching liabilities to assets, index-linked debt hedges the exposure to changes in RPI and delivers a cash flow benefit, as compensation for the inflation risk is provided through adjustment to the principal rather than in cash.

The carrying value of index-linked debt held by the WPD Group is as follows:

	2020 £m	2019 £m
Index-linked debt	902.0	881.9

#### Inflation sensitivity

Assuming sensitivity to the RPI does not take into account any changes to revenue or operating costs that are affected by RPI or inflation generally, the following table shows the illustrative effect on the income statement and items that are recognised directly in equity that would result from reasonably possible movements in changes in RPI before the effects of tax.

	2020		2019	9
	Income statement		Income statement	_
	(before tax) +/- £m	Equity +/- £m	(before tax) +/- £m	Equity +/- £m
UK Retail Prices Index +/- 1.00%	9.0	(7.3)	8.8	(7.1)

## Foreign currency risk

The WPD Group's assets are principally sterling denominated; however, the WPD Group has access to various international debt capital markets and raises foreign currency denominated debt. Where long-term debt is denominated in a currency which is not sterling, the WPD Group's policy is to swap 100% of the foreign currency denominated principal and interest cash flows into sterling through the use of cross-currency swaps.

Under a currency swap, the WPD Group agrees with another party to exchange the principal amount of the two currencies, together with interest amounts in the two currencies agreed by reference to a specific interest rate basis and principal amount. The principal of these instruments reflects the extent of the WPD Group's involvement in the instruments but does not represent its exposure to credit risk, which is assessed by reference to the fair value.

The WPD Group holds an investment of \$200m 2018 6.42% Eurobonds issued by PPL UK Resources Limited which were acquired at a premium of \$21m. During the prior year the maturity date was extended to 2021. It also has borrowings of \$200m under a related committed credit facility. At 31 March 2020, the WPD Group was exposed to movements on exchange rates of \$1.1m (2019: \$1.9m), being the net of the amortised Eurobond investment and dollar borrowings under the committed credit facility.

The principal amount of the WPD Group's foreign currency denominated monetary assets and monetary liabilities at the reporting date and the impact of derivative financial instruments used to manage foreign currency risk were as follows:

For the year ended 31 March 2020

## 24. Financial instruments (continued)

Foreign currency risk (continued)

	2020 \$m	2019 \$m
Investment in parent company Eurobonds	201.1	201.9
Borrowings	(902.0)	(902.0)
Gross exposure	(700.9)	(700.1)
Effect of cross-currency swaps	702.0	702.0
Net exposure	1.1	1.9

#### Foreign currency sensitivity

The following table demonstrates the sensitivity to a reasonably possible change in Sterling against the US dollar exchange rate, with all other variables held constant, of the WPD Group's profit before tax and the WPD Group's equity.

	2020		2019	)
	Income statement		Income statement	_
	(before tax)	Equity	(before tax)	Equity
	£m	£m	£m	£m
10% increase in exchange rates	(0.1)	(9.3)	(0.1)	(7.6)
10% decrease in exchange rates	0.1	11.4	0.2	9.4

#### Credit risk (see also Note 18)

Credit risk is the risk that a customer or counterparty to a financial instrument will fail to perform or fail to pay amounts due causing financial loss to the WPD Group and arises from cash and cash equivalents, derivative financial instruments and deposits with financial institutions and principally from credit exposures to customers relating to outstanding receivables.

WPD maintains credit policies and procedures with respect to counterparties (including requirements that counterparties maintain certain credit ratings criteria). Depending on the creditworthiness of the counterparty, the WPD Group may require collateral or other credit enhancements such as cash deposits or letters of credit and parent company guarantees.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet. At 31 March the maximum exposure to credit risk was as follows:

•	2020	2019
	£m	£m
Cash and short-term deposits	201.0	142.7
Trade receivables	275.9	261.2
Other receivables	5.7	7.8
Accrued income	6.2	9.9
Investment at amortised cost	161.9	154.9
Derivative financial instruments	163.5	102.9
	814.2	679.4

The table above does not take into account collateral held in relation to trade receivables in the form of cash £2.2m (2019: £2.2m), letters of credit £53.3m (2019: £57.0m), and parent company guarantees £61.3m (2019: £54.5m).

WPD has concentrations of customers among electric utilities and other energy marketing and trading companies. These concentrations of counterparties may impact WPD's overall exposure to credit risk, either positively or negatively, in that counterparties may be similarly affected by changes in economic, regulatory or other conditions.

For the year ended 31 March 2020

## 24. Financial instruments (continued)

Credit risk (see also Note 18) (continued)

The analysis of WPD's financial assets by credit risk rating grade is as follow:

The analysis of WLD's infancial assets by credit fisk i	12 month	Lifetime			
2020	ECL	ECL	FVTPL	FVOCI	Total
2020	£m	£m	£m	£m	£m
	æm	æm	æm	æm	æm
AAA to A (Low to Fair Risk)	64.4	-	136.6	163.5	364.5
BBB+ to B (Monitoring)	-	-	-	-	-
CCC and below (Substandard)	162.0	-	-	-	162.0
Others monitored on ageing matrix	-	290.8	-	-	290.8
Total gross carrying value	226.4	290.8	136.6	163.5	817.3
Loss allowance	(0.1)	(3.0)	-	-	(3.1)
Net carrying value	226.3	287.8	136.6	163.5	814.2
2019	12 month	Lifetime			
201)	ECL	ECL	FVTPL	FVOCI	Total
	£m	£m	£m	£m	£m
AAA to A (Low to Fair Risk)	52.8	_	89.9	102.9	245.6
BBB+ to B (Monitoring)	52.6	_	-	102.9	243.0
CCC and below (Substandard)	155.0	_	_	_	155.0
Others monitored on ageing matrix	-	282.2	-	-	282.2
Total Gross Carrying Value	207.8	282.2	89.9	102.9	682.8
Loss Allowance	(0.1)	(3.3)	-	-	(3.4)
Net Carrying Value	207.7	278.9	89.9	102.90	679.4

## Liquidity risk

Liquidity risk is the risk that the WPD Group will not have sufficient funds to meet the obligations or commitments arising from its business operations and its financial liabilities.

Treasury is responsible for managing the banking and liquidity requirements of the WPD Group, risk management relating to interest rate and foreign exchange exposures, and for managing the credit risk relating to the banking counterparties with which it transacts. The department's operations are governed by policies determined by the Board.

The following credit facilities were in place at 31 March 2020:

	Expiration Capacity		Borrowed	Letters of credit issued	Unused capacity
	date	£m	£m	£m	£m
WPD plc - Syndicated Credit Facility	Jan. 2023	210.0	161.0	-	49.0
WPD South West - Syndicated Credit Facility	July 2021	245.0	100.0	-	145.0
WPD East Midlands - Syndicated Credit Facility	July 2021	300.0	-	-	300.0
WPD West Midlands - Syndicated Credit Facility	<b>July 2021</b>	300.0	-	-	300.0
Uncommitted Credit Facilities		100.0	-	3.5	96.5
Total Credit Facilities		1,155.0	261.0	3.5	890.5

For the year ended 31 March 2020

## 24. Financial instruments (continued)

#### Liquidity risk (continued)

The WPD Group's primary source of liquidity is cash generated from its ongoing business operations. The electricity regulator sets a major element of the WPD Group's revenues, providing both a stable and predictable source of funds. In recognition of the long life of the WPD Group's assets and anticipated indebtedness, and to create financial efficiencies, the WPD Group's policy is to arrange that debt maturities are spread over a wide range of dates, thereby ensuring that the WPD Group is not subject to excessive refinancing risk in any one year. The WPD Group has entered into borrowing agreements for periods out to 2056.

The following tables detail the WPD Group's remaining contractual maturity for its non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the WPD Group can be required to pay. The table includes both interest and principal cash flows.

2020	Less than one year £m	One to five years £m	Five to fifteen years £m	Greater than fifteen years £m	Total £m
Borrowings Lease liabilities Trade and other payables	703.6 1,553.0 348.7	2,967.5 4,764.0	3,724.8 3,973.0	2,935.1 6,703.0	10,331.0 16,993.0 348.7
Total	2,605.3	7,731.5	7,697.8	9,638.1	27,672.7
2019	Less than one year £m	One to five years £m	Five to fifteen years £m	Greater than fifteen years £m	Total £m
Borrowings Trade and other payables Total	535.3 340.3 875.6	2,713.0 - 2,713.0	3,961.0 - 3,961.0	3,476.8	10,686.1 340.3 11,026.4

The following table details the WPD Group's liquidity analysis for its derivative financial instruments. The table has been drawn up based on the undiscounted gross cash (inflows) and outflows on derivatives that require gross settlement.

2020	Less than one year £m	One to five years £m	Five to fifteen years £m	Greater than fifteen years £m	Total £m
Cross currency derivative payments Cross currency derivative receipts	26.3 (33.6)	351.4 (461.4)	157.8 (210.6)	- -	535.5 (705.6)
Total	(7.3)	(110.0)	(52.8)	-	(170.1)
2019	Less than one year £m	One to five years £m	Five to fifteen years £m	Greater than fifteen years £m	Total £m
Cross currency derivative payments Cross currency derivative receipts	26.3 (32.0)	368.7 (460.2)	166.8 (212.1)	-	561.8 (704.3)
Total	(5.7)	(91.5)	(45.3)	-	(142.5)

 $Fair\ values\ of\ financial\ assets\ and\ financial\ liabilities$ 

Set out below is a comparison by category of carrying amounts and fair values of all of the WPD Group's financial instruments that are carried in the financial statements.

For the year ended 31 March 2020

## 24. Financial instruments (continued)

Fair values of financial assets and financial liabilities (continued)

2020	Amortised cost £m	Fair value through profit & loss £m	Fair value through OCI £m	Total book value £m	Fair value £m
	£111	žIII	ziii	ziii	žiii
Financial assets					
Cash	64.4	136.6	-	201.0	201.0
Investment at amortised cost	161.9	-	-	161.9	178.5
Derivative financial instruments	-	-	163.5	163.5	163.5
Trade and other receivables	287.8	-	-	287.8	287.8
Financial liabilities					
Bank overdraft	(13.5)	-	-	(13.5)	(13.5)
Interest-bearing loans and borrowings:					
- Floating rate borrowings	(261.1)	-	-	(261.1)	(261.1)
- Fixed rate borrowings	(5,360.6)	-	-	(5,360.6)	(6,241.6)
- Index linked	(902.0)	-	-	(902.0)	(1,294.0)
Derivative financial instruments	-	-	(4.9)	(4.9)	(4.9)
Lease liabilities	(10.1)			(10.1)	(10.1)
Trade and other payables	(348.7)	-	-	(348.7)	(348.7)
	(6,381.9)	136.6	158.6	(6,086.7)	(7,343.1)
2019		Fair value			
		though	Fair value		
	Amortised	profit &	through	Total book	
	cost	loss	OCI	value	Fair value
			£m	£m	£m
	£m	£m	LIII	LIII	2111
Financial assets	£m	£m	žIII.	LIII	ZIII
Financial assets Cash	£m 52.8	£m 89.9	-	142.7	142.7
			- -		
Cash	52.8		- 102.9	142.7	142.7
Cash Investment at amortised cost	52.8		-	142.7 154.9	142.7 184.5
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities	52.8 154.9 - 278.9		-	142.7 154.9 102.9 278.9	142.7 184.5 103.0 278.9
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft	52.8 154.9		-	142.7 154.9 102.9	142.7 184.5 103.0
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings:	52.8 154.9 - 278.9		-	142.7 154.9 102.9 278.9	142.7 184.5 103.0 278.9
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings: - Floating rate borrowings	52.8 154.9 - 278.9 (19.5) (244.0)		-	142.7 154.9 102.9 278.9 (19.5)	142.7 184.5 103.0 278.9 (19.5)
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings: - Floating rate borrowings - Fixed rate borrowings	52.8 154.9 - 278.9 (19.5) (244.0) (5,037.6)		-	142.7 154.9 102.9 278.9 (19.5) (244.0) (5,037.6)	142.7 184.5 103.0 278.9 (19.5) (244.0) (5,706.3)
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings: - Floating rate borrowings - Fixed rate borrowings - Index linked	52.8 154.9 - 278.9 (19.5) (244.0)		- 102.9 -	142.7 154.9 102.9 278.9 (19.5) (244.0) (5,037.6) (881.9)	142.7 184.5 103.0 278.9 (19.5) (244.0) (5,706.3) (1,262.3)
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings: - Floating rate borrowings - Fixed rate borrowings - Index linked Derivative financial instruments	52.8 154.9 - 278.9 (19.5) (244.0) (5,037.6) (881.9)		-	142.7 154.9 102.9 278.9 (19.5) (244.0) (5,037.6) (881.9) (2.8)	142.7 184.5 103.0 278.9 (19.5) (244.0) (5,706.3) (1,262.3) (2.8)
Cash Investment at amortised cost Derivative financial instruments Trade and other receivables  Financial liabilities Bank overdraft Interest-bearing loans and borrowings: - Floating rate borrowings - Fixed rate borrowings - Index linked	52.8 154.9 - 278.9 (19.5) (244.0) (5,037.6)		- 102.9 -	142.7 154.9 102.9 278.9 (19.5) (244.0) (5,037.6) (881.9)	142.7 184.5 103.0 278.9 (19.5) (244.0) (5,706.3) (1,262.3)

The fair value of the WPD Group's outstanding cross currency swaps is the estimated amount, calculated using discounted cash flow models, that the WPD Group would receive or pay in order to terminate such contracts in an arm's length transaction taking into account market rates of interest and foreign exchange at the balance sheet date.

The carrying value of the WPD Group's bank loans and overdrafts approximates their fair value. The fair value of the WPD Group's other borrowings is estimated using quoted prices or, where these are not available, discounted cash flow analyses based on the WPD Group's current incremental borrowing rates for similar types and maturities of borrowing: these are classified as Level 2 in the fair value hierarchy.

For the year ended 31 March 2020

### 24. Financial instruments (continued)

Fair values of financial assets and financial liabilities (continued)

The carrying value of short term receivables and payables are assumed to approximate their fair values where discounting is not material.

Fair value hierarchy

The WPD Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

As at 31 March 2020, the WPD Group held the following financial instruments measured at fair value:

2020	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets measured at fair value			3411	
Derivatives financial instruments	-	163.5	-	163.5
Short term deposits	136.6	-	-	136.6
2019	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
Assets measured at fair value				
Derivatives financial instruments	-	102.9	-	102.9
Short term deposits	89.9	-	-	89.9

To manage interest rate risk, WPD uses interest rate contracts such as forward-starting swaps. To manage foreign currency exchange risk, WPD uses foreign currency contracts such as cross-currency swaps. An income approach is used to measure the fair value of these contracts, utilising readily observable inputs, such as forward interest rates and forward foreign currency exchange rates, as well as inputs that may not be observable, such as credit valuation adjustments. In certain cases, market information cannot practicably be obtained to value credit risk and therefore internal models are relied upon. These models use projected probabilities of default and estimated recovery rates based on historical observances. The impact of credit risk on the fair value of derivatives is generally small relative to liabilities like debt, because the principal (notional) amount is not at risk and credit enhancements often exist and thus the overall classification of derivatives as Level 2 remains appropriate. WPD generally does not calculate separate liquidity valuation adjustments, based on the traders' view that liquidity risk is included in the market prices. WPD also does not generally calculate modelling reserves, as the interest rate/foreign currency derivatives can be developed using standard practices.

During the reporting period ending 31 March 2020, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of the Level 3 fair value measurements.

Hedge counterparties are major banks of high quality credit standing.

In addition to the above financial instruments, the fair value of long-term debt and investment at amortised cost as disclosed under financial liabilities is classified as Level 2.

WPD uses observable market data from Bloomberg to arrive at the fair value of long term debt and investment at amortised cost.

For the year ended 31 March 2020

## 24. Financial instruments (continued)

#### Capital risk management

The primary objective of the WPD Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise shareholder value.

The WPD Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the WPD Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policies or processes during the years ended 31 March 2020 or 31 March 2019.

The WPD Group does not consider the standard gearing ratio of net debt as a percentage of net debt plus net assets shown in the balance sheet as an appropriate capital monitoring measure as it does not reflect the economic value of the assets of the Group's regulated businesses. Instead, the WPD Group monitors capital using a gearing ratio, which is net debt divided by the RAV. The RAV is a regulatory measure of the regulated business' asset base required to carry out the regulated activities. Regulated revenues are designed to cover operating costs (including certain replacement expenditure) and capital depreciation, as well as an allowed return on the RAV. The WPD Group's policy is to maintain a gearing ratio that ensures an investment grade credit rating. The WPD Group includes within net debt borrowings and associated cross currency swaps less cash and cash equivalents and deposits.

	2020	2019
	£m	£m
Chart tamp homorpings	426.2	262.5
Short term borrowings		263.5
Long term borrowings Lease liabilities	6,111.0 10.1	5,919.5
		2.5
Letters of credit	3.5	3.5
Cross currency swaps	(163.1)	(102.8)
Cash at bank and in hand (excluding restricted cash)	(187.8)	(128.5)
Net debt	6,199.9	5,955.2
Regulatory Asset Value	7,999.7	7,698.1
Gearing ratio	78%	77%
Reconciliation of cash flows to net debt	2020	2019
	£m	£m
Net (increase)/decrease in cash at hand in bank	(59.3)	33.5
Net increase/(decrease) in short term borrowings	3.0	(195.1)
Net increase in long term borrowings	295.0	375.4
Payment of lease liabilities	(1.5)	<u> </u>
Change in debt resulting from cash flows	237.2	213.8
Net increase in derivatives	(60.3)	(53.2)
Foreign exchange loss on borrowings	34.8	48.9
Net increase in borrowings due to indexation	22.3	20.0
Amortisation of premiums, discounts and issue costs	(0.9)	(1.6)
Leases acquired during the year	11.3	(1.0)
Interest expense on lease	0.3	_
interest expense on rease	0.3	
Movement in net debt in the year	244.7	227.9
Net debt at beginning of year	5,955,2	5,727.3
Net debt at end of year	6,199.9	5,955.2

For the year ended 31 March 2020

### 25. Derivative financial instruments

#### Cross-currency swaps

The WPD Group entered into cross-currency interest rate swaps designated as cash flow hedges in order to hedge the currency cash flow risks associated with the future interest and principal payments on the WPD Group's US dollar borrowings arising from fluctuations in currency rates.

The cross-currency swaps have two fixed interest rate legs that match the interest, payment debts, currency, notional amount and maturity date of USD denominated debt and thus no ineffectiveness is expected. Furthermore, the swaps also provide for a final exchange of currency on maturity of debts, thereby also eliminating any currency risk related to the principal repayment.

The assessment of whether the derivative will be highly effective is determined by comparison of the critical terms of the hedging instrument (i.e. cross-currency interest rate swap) with the critical terms of the hedged item. Because of the fact that the critical terms are the same (timing and amount of US dollar cash flows), the entity can conclude that changes in cash flows attributable to the risk being hedged are expected to be completely offset by the hedging derivative. The only possible source of hedge ineffectiveness is the credit risk of the swap counterparty. There has been no adverse development with regard to the counterparty's credit risk.

The hedge ratio is calculated from the quantity of the hedge item being hedged and the quantity of the hedging instrument being used to hedge that quantity of the hedged item. There is no imbalance between the weightings of the hedged item and the hedging instrument.

At 31 March 2020, the WPD Group had outstanding cross-currency swap agreements in cash flow hedges against borrowings with a total principal amount of \$702.0m (2019: \$702.0m) and a swapped notional principal of £428.8m (2019: £428.8m). The hedges were assessed to be highly effective. The cross-currency swaps have a remaining term ranging from one to eight years (2019: two to nine years) to match the underlying hedged borrowings consisting of semi-annual interest payments and the repayment of principal amounts. Under the swaps the WPD Group receives US dollar interest at an average fixed rate of 6.0% (2019: 6.0%) and pays pound sterling interest at an average fixed rate of 6.1% (2019: 6.1%).

#### Forward-starting interest rate swaps

WPD wishes to hedge the variability in the semi-annual interest payments related to the forecast debt issuance attributable to changes in the benchmark interest rate (i.e. swap rate) between hedge inception and the issuance's pricing date. This can be achieved through the use of a forward-starting interest rate swap, whereby WPD pays fixed and receives floating, that will be terminated when the debt issuance is priced. Through interest rate swaps WPD wants to benefit from lower gilt rates at a point of time. Locking in the rates at the lowest possible levels assists WPD to outperform the allowed cost of debt under Ofgem's price control mechanism.

The assessment of whether the hedge is effective is determined by using regression techniques to produce a comparison of the hedging instrument (forward starting interest rate swap) with the hedged item (forecast debt issuance).

The possible sources of hedge ineffectiveness are if the hedged transaction does not occur or if the transaction does not occur at the initial agreed terms such as timing, principal and tenor of issuance. Another possible source of hedge ineffectiveness is the credit risk of the swap counterparty.

The hedge ratio is calculated from the quantity of the hedge item being hedged and the quantity of the hedging instrument being used to hedge that quantity of the hedged item. There is no imbalance between the weightings of the hedged item and the hedging instrument.

For the year ended 31 March 2020

# 25. Derivative financial instruments (continued)

Hedging instruments

As at 31 March, the WPD Group held the following derivative financial instruments measured at fair value:

2020					Change in fair value
	Nominal amount £m	Carrying amount (assets) £m	Carrying amount (liabilities) £m	Line item in balance sheet £m	relevant to ineffective hedge £m
Foreign currency risk					
Cross-currency swaps - cash flow hedges	428.8	163.1	-	Derivative financial instruments	-
Interest rate risk Interest rate swaps - cash flow hedges	125.5	0.4	4.9	Derivative financial instruments	-
	554.3	163.5	4.9	-	-
2019					Change in fair value
	Nominal	Carrying	Carrying	Line item	relevant to
	Nominal amount	amount (assets)	amount (liabilities)	in balance sheet	ineffective hedge
	£m	£m	£m	£m	£m
Foreign currency risk					
Cross-currency swaps - cash flow hedges	428.8	102.8	-	Derivative financial instruments	-
Interest rate risk Interest rate swaps - cash flow hedges	300.0	0.1	2.8	Derivative financial instruments	-
	728.8	102.9	2.8	-	-
Timing profile for hedge instruments' nominal amounts			2020		
	Less than	One to	2020 Five to	Greater than	
	one year £m		fifteen years £m		Total £m
Cross-currency swaps - cash flow hedge Interest rate swaps - cash flow hedge	125.5	306.9	121.9	- -	428.8 125.5
	Less than one year £m	One to five years £m	2019 Five to fifteen years £m	Greater than fifteen years £m	Total £m
Cross-currency swaps - cash flow hedge Interest rate swaps - cash flow hedge	300.0	306.9	121.9	-	428.8 300.0

For the year ended 31 March 2020

# 25. Derivative financial instruments (continued)

Hedging instruments (continued)

The average rate of the hedging instruments is as follows:

	ments is as follows:			2020		2019
Foreign currency risk						
Cross-currency swaps				6.13%		6.13%
Interest rate risk						
Interest rate swaps				0.89%		1.48%
Hedged items						
o de la companya de		2	020		20	019
		Value			Value	
		change			change	
		in hedged	Cash flow		in hedged	Cash flow
		item relating	hedge		item relating	hedge
		to hedge	reserve		to hedge	reserve
	ir	neffectiveness	balance	i	neffectiveness	balance
Essaisa araman araida		£m	£m		£m	£m
Foreign currency risk			23.8			(7.0)
Foreign currency borrowings		-	23.0		-	(7.9)
Interest currency risk						
Borrowings		-	(22.6)		-	2.7
Hedge effectiveness						
Treage egyeenveness			2	020		
			Line item in			
			income	Amount	A mount	Line item in
				Amount	Amount	Line item in
		Ineffective	statement	reclassified	reclassified	income
	ŀ	Ineffective nedge portion				
	ł Hedging		statement	reclassified	reclassified	income
		nedge portion	statement including	reclassified because	reclassified because	income statement
	Hedging gain/(loss) in OCI	nedge portion recognised in income statement	statement including ineffective	reclassified because cash flows	reclassified because hedged item	income statement including
	Hedging gain/(loss)	nedge portion recognised in income	statement including ineffective hedge	reclassified because cash flows no longer	reclassified because hedged item affected	income statement including reclass
Foreign currency risk	Hedging gain/(loss) in OCI	nedge portion recognised in income statement	statement including ineffective hedge	reclassified because cash flows no longer expected	reclassified because hedged item affected P&L	income statement including reclass
Foreign currency risk Interest rate risk	Hedging gain/(loss) in OCI £m	nedge portion recognised in income statement	statement including ineffective hedge	reclassified because cash flows no longer expected	reclassified because hedged item affected P&L £m	income statement including reclass adjustment
- ·	Hedging gain/(loss) in OCI £m	nedge portion recognised in income statement	statement including ineffective hedge portion	reclassified because cash flows no longer expected	reclassified because hedged item affected P&L £m	income statement including reclass adjustment
- ·	Hedging gain/(loss) in OCI £m	nedge portion recognised in income statement	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m	income statement including reclass adjustment
- ·	Hedging gain/(loss) in OCI £m	nedge portion recognised in income statement £m	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4	income statement including reclass adjustment
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)	recognised in income statement £m	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4	income statement including reclass adjustment Finance costs
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)	recognised in income statement £m	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because	income statement including reclass adjustment  Finance costs  Line item in income statement
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)	Ineffective hedge portion recognised	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item	income statement including reclass adjustment  Finance costs  Line item in income statement including
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)  Hedging gain / (loss)	Ineffective hedge portion recognised in income	statement including ineffective hedge portion  2 Line item in income statement including ineffective hedge	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item affected	income statement including reclass adjustment  Finance costs  Line item in income statement including reclass
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)  Hedging gain / (loss) in OCI	Ineffective hedge portion recognised in income statement £m	statement including ineffective hedge portion	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item affected P&L	income statement including reclass adjustment  Finance costs  Line item in income statement including
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)  Hedging gain / (loss)	Ineffective hedge portion recognised in income	statement including ineffective hedge portion  2 Line item in income statement including ineffective hedge	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item affected	income statement including reclass adjustment  Finance costs  Line item in income statement including reclass
Interest rate risk	Hedging gain/(loss) in OCI £m  59.2 (25.7)  Hedging gain / (loss) in OCI £m	Ineffective hedge portion recognised in income statement £m	statement including ineffective hedge portion  2 Line item in income statement including ineffective hedge	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item affected P&L £m	income statement including reclass adjustment  Finance costs  Line item in income statement including reclass adjustment
- ·	Hedging gain/(loss) in OCI £m  59.2 (25.7)  Hedging gain / (loss) in OCI	Ineffective hedge portion recognised in income statement £m	statement including ineffective hedge portion  2 Line item in income statement including ineffective hedge	reclassified because cash flows no longer expected £m	reclassified because hedged item affected P&L £m  (27.5) 0.4  Amount reclassified because hedged item affected P&L	income statement including reclass adjustment  Finance costs  Line item in income statement including reclass

For the year ended 31 March 2020

## 25. Derivative financial instruments (continued)

Reconciliation of cash flow hedge reserve

	2020	2019
	£m	£m
Opening balance	(5.2)	(17.9)
Hedging gain	33.5	48.5
Amount reclassified to income statement because		
cash flows no longer expected	-	-
Amount reclassified to income statement because		
hedged item affected profit and loss	(27.1)	(35.8)
Closing balance	1.2	(5.2)

#### 26. Deferred tax

The following are the deferred tax liabilities and assets recognised by the WPD Group and movements thereon during the current and prior year:

	Accelerated capital	Retirement benefit		
	allowances	obligation	Other	Total
	£m	£m	£m	£m
At 1 April 2018	554.6	(33.8)	(22.0)	498.8
Charge to the income statement	35.2	25.3	5.0	65.5
Charge to equity	-	25.4	2.5	27.9
At 1 April 2019	589.8	16.9	(14.5)	592.2
Charge to the income statement	93.1	29.5	2.6	125.2
Charge to equity		66.7	1.4	68.1
At 31 March 2020	682.9	113.1	(10.5)	785.5

Certain deferred tax assets and liabilities have been offset. The following is an analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2020	2019
	£m	£m
Deferred tax liabilities	861.3	681.6
Deferred tax assets	(75.8)	(89.4)
Net deferred tax liabilities	785.5	592.2

The net deferred tax liability due after more than one year is £790.7m (2019: £610.2m).

Deferred tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the deferred tax benefit through future taxable profits is probable. The WPD Group did not recognise deferred tax assets of £181.1m (2019: £162.1m) in respect of capital losses amounting to £953.0m (2019: £953.6m) that can be carried forward against future taxable chargeable gains as there is no use of these assets for the foreseeable future.

For the year ended 31 March 2020

## 27. Retirement benefit obligations

#### Introduction

The WPD Group operates four defined benefit pension schemes:

- two segments of the Electricity Supply Pension Scheme ("ESPS"),
  - the segment covering WPD South West and WPD South Wales ("ESPS WPD"), and
  - the segment covering WPD East Midlands and WPD West Midlands ("ESPS CN")
- the Western Power Utilities Pension Scheme ("WPUPS")
- the Infralec 1992 Pension Scheme ("Infralec 92")

The assets of all four schemes are held separately from those of the WPD Group in trustee administered funds.

The ESPS provides pension and other related defined benefits based on final pensionable pay to employees throughout the electricity supply industry. The two segments of the ESPS relating to WPD are closed to new members except in very limited circumstances. Existing members are unaffected. A defined contribution scheme is offered to new employees.

WPD South Wales is the principal employer for WPUPS, which is a defined benefit scheme providing benefits relating to previous employees of an affiliate group which was previously headed by Hyder plc (now Hyder Limited in liquidation). WPD South Wales will fund the actuarial deficit. However, as PPL WPD Limited, the Company's parent, has taken full financial responsibility for this scheme, WPD South Wales will be reimbursed for these payments. As PPL WPD Limited is outside the WPD Group, the value of the reimbursement agreement is stated in the balance sheet (Note 28) and matches the gross asset/liability recorded under IAS 19 below.

Infralec 92 provides benefits on both a money purchase and final salary basis and is operated by WPD South Wales.

WPUPS and Infralec 92 are closed to active members.

The WPD Group also has an unfunded obligation which relates to previous executives of WPD East Midlands and WPD West Midlands.

### Other scheme

WPD also operates a defined contribution scheme. The assets of the scheme are held separately from those of WPD in an independent fund administered by the scheme trustee. The scheme has two sections:

- (a) a closed section with no active members. At 31 March 2020 there were 198 members with deferred benefits in the scheme (2019: 199) and 4 pensioners (2019: 5). Market value of the assets was £1.9m (2019: £2.1m).
- (b) a new pension arrangement available to all new employees in WPD with effect from 1 April 2010. At 31 March 2020 there were 4,058 members (2019: 3,767). The market value of the assets of the open section of the scheme was £97.0m (2019: £89.2m). Employer contributions to the scheme amounted to £9.7m in the year (2019: £8.6m).

#### Defined benefit schemes

The liability/asset recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of the plan assets. The defined benefit obligation is calculated annually by independent actuaries, Aon Hewitt Limited, using the projected unit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits are paid, and that have terms to maturity approximating to the terms of the related pension obligation.

Actuarial gains and losses arising from experience adjustments and changes to actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in income.

The schemes are funded, defined benefit, final salary pension plans. The level of benefits provided depends on members' length of service and their salary at their date of leaving the WPD. The majority of pensions in payment receive inflationary increases in line with the RPI ("Retail Prices Index") inflation. The benefit payments are from trustee-administered funds. The amount of contributions to be paid is decided jointly by the employer and the Trustees of the Scheme. Assets held in trust are governed by UK regulations and practice. The schemes' investment strategy is decided by the Trustees, in consultation with the employer. The Boards of Trustees must be composed of representatives of the employer and plan participants in accordance with the schemes' legal documentation.

For the year ended 31 March 2020

## 27. Retirement benefit obligations (continued)

The amounts recognised in the balance sheet are determined as follows:

	2020							
	ESPS WPD				Total			
	£m	£m	£m	£m	£m	£m		
Present value of obligations	2,283.9	3,263.4	476.1	12.6	4.3	6,040.3		
Fair value of scheme assets	(2,414.7)	(3,580.2)	(625.5)	(15.1)	-	(6,635.5)		
(Surplus)/deficit of funded plan and liability/ (asset) recognised in the balance sheet	(130.8)	(316.8)	(149.4)	(2.5)	4.3	(595.2)		
Represented by:								
Retirement benefit obligations	-		-	-	4.3	4.3		
Retirement benefit assets	(130.8)	(316.8)	(149.4)	(2.5)	-	(599.5)		
	(130.8)	(316.8)	(149.4)	(2.5)	4.3	(595.2)		
			201	9				
	ESPS WPD	ESPS CN	WPUPS	Infralec 92	Unfunded	Total		
	£m	£m	£m	£m	£m	£m		
Present value of obligations	2,474.2	3,523.3	525.4	13.3	4.6	6,540.8		
Fair value of scheme assets	(2,422.5)	(3,584.6)	(623.3)	(15.9)	-	(6,646.3)		
Deficit/(surplus) of funded plan and liability/ (asset) recognised in the balance sheet	51.7	(61.3)	(97.9)	(2.6)	4.6	(105.5)		
Represented by:								
Retirement benefit obligations	-	- (61.0)	- (07.0)	-	4.6	4.6		
Retirement benefit assets	51.7	(61.3)	(97.9)	(2.6)	-	(110.1)		
	51.7	(61.3)	(97.9)	(2.6)	4.6	(105.5)		

The regulator, Ofgem, currently allows ongoing service costs and a proportion of the deficit costs to be recovered through regulated income.

Analysis of the amount charged to profit before interest and taxation or to capital expenditure:

	2020						
	ESPS WPD £m	ESPS CN	WPUPS	Infralec 92	Unfunded	Total	
		£m	£m	£m	£m	£m	
Current service cost	30.1	32.4	-	-	-	62.5	
Administrative costs	1.4	2.2	0.6	-	-	4.2	
WPUPS reimbursement agreement	-	-	(0.6)	-	-	(0.6)	
Operating charge relating to defined benefit plans	31.5	34.6	-	-	-	66.1	
Interest income on plan assets	(57.3)	(84.1)	(14.4)	(0.4)	-	(156.2)	
Interest on plan liabilities	57.6	81.8	12.1	0.3	0.1	151.9	
WPUPS reimbursement agreement	-	-	2.3	-	-	2.3	
Other finance income	0.3	(2.3)	-	(0.1)	0.1	(2.0)	

For the year ended 31 March 2020

# 27. Retirement benefit obligations (continued)

	2019					
	ESPS WPD £m	ESPS CN	WPUPS	Infralec 92	Unfunded	Total
		£m	£m	£m	£m	£m
Current service cost	29.6	31.7	-	_	-	61.3
Administrative costs	1.3	1.7	0.4	-	-	3.4
Past service cost and gains and losses						
on settlement*	2.5	7.0	4.2			13.7
WPUPS reimbursement agreement	-	-	(4.6)	-	-	(4.6)
Operating charge relating to defined benefit plans	33.4	40.4	-	-	-	73.8
Interest income on plan assets	(58.3)	(86.7)	(15.2)	(0.4)	-	(160.6)
Interest on plan liabilities	61.4	87.9	13.3	0.3	0.1	163.0
WPUPS reimbursement agreement	-	-	1.9	-	-	1.9
Other finance expense	3.1	1.2	-	(0.1)	0.1	4.3

<sup>\*</sup> Following the High Court ruling in October 2018, a Guaranteed Minimum Pension ("GMP") equalisation is required and various methods are permissible for the same. £13.7m represents the Group's estimate of likely additional pension liabilities using the default Method C2 for equalising for the effect of GMP.

The operating charge is allocated to the operating expenses in the income statement or to capital expenditure as appropriate.

Analysis of the amount recognized in other comprehensive income:

Analysis of the amount recognized in other c	2020						
	ESPS WPD	ESPS CN	WPUPS	Infralec 92	Unfunded	Total	
	£m	£m	£m	£m	£m	£m	
Return on plan assets excluding amounts							
included in interest income	77.8	43.3	(13.5)	0.7	-	108.3	
(Gain)/loss from change in							
demographic assumptions	(12.5)	-	5.4	-	-	<b>(7.1)</b>	
Gain from change in							
financial assumptions	(189.9)	(243.7)	(22.6)	(0.6)	(0.2)	(457.0)	
Experience losses/(gains)	21.4	17.7	(19.1)	0.1	-	20.1	
MEPS DC bulk transfer**	-	1.0	-	-	-	1.0	
WPUPS reimbursement agreement	-	-	49.8	-	-	49.8	
Remeasurement (gains)/losses recognised in other comprehensive income	(103.2)	(181.7)	-	0.2	(0.2)	(284.9)	
			201	19			
	ESPS WPD	ESPS CN	WPUPS	Infralec 92	Unfunded	Total	
	£m	£m	£m	£m	£m	£m	
Return on plan assets excluding amounts							
included in interest income	(91.5)	(157.6)	(33.6)	(0.8)	-	(283.5)	
Gain from change in							
demographic assumptions	(94.4)	(131.2)	(18.6)	(0.5)	-	(244.7)	
Loss from change in				, ,		, ,	
financial assumptions	136.1	193.2	26.6	0.7	-	356.6	
		4-0	(0.0)	0.1		27.8	
Experience losses/(gains)	13.3	15.2	(0.8)	0.1	-	21.0	
Experience losses/(gains) WPUPS reimbursement agreement	13.3	15.2	26.4	-	-	26.4	

For the year ended 31 March 2020

## 27. Retirement benefit obligations (continued)

The movement in the net defined benefit obligation over the accounting period is as follows:

ESPS WPD	Year ended 31 March 2020			Year ended 31 March 2019		
<del></del>	Present	Fair value		Present	Fair value	
	value of	of plan		value of	of plan	
	obligation	assets	Total	obligation	assets	Total
	£m	£m	£m	£m	£m	£m
Liability/(asset) at 1 April	2,474.2	(2,422.5)	51.7	2,416.6	(2,253.6)	163.0
Current service cost	30.1	-	30.1	29.6	-	29.6
Administrative costs	1.4	-	1.4	1.3	-	1.3
Interest expense/(income)	57.6	(57.3)	0.3	61.4	(58.3)	3.1
Past service cost and gains and losses						
on settlements	-	-	-	2.5		2.5
	89.1	(57.3)	31.8	94.8	(58.3)	36.5
Remeasurements:						
Return on plan assets excluding amounts						
included in interest expense/(income)	_	77.8	77.8	_	(91.5)	(91.5)
Gain from change in					( /	( )
demographic assumptions	(12.5)	_	(12.5)	(94.4)	_	(94.4)
(Gain)/loss from change in	(==::)		(====)	(5)		(>)
financial assumptions	(189.9)	_	(189.9)	136.1	_	136.1
Experience losses	21.4	_	21.4	13.3	_	13.3
r · · · · · · · · · · · · · · · · · · ·	(181.0)	77.8	(103.2)	55.0	(91.5)	(36.5)
Contributions:						
Employers	_	(111.1)	(111.1)	_	(111.5)	(111.5)
Plan participants	4.2	(4.2)	-	4.2	(4.2)	-
1 mi puite puite	4.2	(115.3)	(111.1)	4.2	(115.7)	(111.5)
Payments from plan:						
Benefit payments	(101.2)	101.2	-	(105.5)	105.5	_
Administrative costs	(1.4)	1.4	-	(1.3)	1.3	-
Acquired in a business combination*			_	10.4	(10.2)	0.2
Acquired in a business combination	(102.6)	102.6	<u>-</u>	(96.4)	96.6	0.2
	(102.0)	102.0	<del>-</del>	(90.4)	90.0	0.2
Liability/(asset) at 31 March	2,283.9	(2,414.7)	(130.8)	2,474.2	(2,422.5)	51.7

<sup>\*</sup> Following the event of insolvency of Carillion in January 2018, 39 former South Wales Electricity Board ("SWALEC") employees (now retired), with certain rights under the Protected Persons Regulations, were transferred to the WPD Group ESPS on 29 March 2019. Following the transfer, an amount of £10.2m, representing a proportionate share of the Carillion Group ESPS Pension Scheme's assets, was transferred to the WPD Group ESPS bank account.

For the year ended 31 March 2020

# 27. Retirement benefit obligations (continued)

ESPS CN	Year ended 31 March 2020			Year ended 31 March 2019		
	Present	Fair value		Present	Fair value	
	value of	of plan		value of	of plan	
	obligation	assets	Total	obligation	assets	Total
	£m	£m	£m	£m	£m	£m
Liability/(asset) at 1 April	3,523.3	(3,584.6)	(61.3)	3,463.5	(3,384.4)	79.1
Current service cost	32.4	-	32.4	31.7	-	31.7
Administrative costs	2.2	-	2.2	1.7	-	1.7
Interest expense/(income)	81.8	(84.1)	(2.3)	87.9	(86.7)	1.2
Past service cost and gains and losses on						
settlement	-	-	-	7.0	-	7.0
	116.4	(84.1)	32.3	128.3	(86.7)	41.6
Remeasurements:						
Return on plan assets excluding amounts						
included in interest (income)/expense	-	43.3	43.3	-	(157.6)	(157.6)
Gain from change in						
demographic assumptions	-		-	(131.2)		(131.2)
(Gain)/loss from change in						
financial assumptions	(243.7)	-	(243.7)	193.2	-	193.2
Experience losses	17.7	-	17.7	15.2	-	15.2
	(226.0)	43.3	(182.7)	77.2	(157.6)	(80.4)
Contributions:						
Employers	-	(106.1)	(106.1)	-	(101.6)	(101.6)
Plan participants	5.5	(5.5)	-	5.5	(5.5)	-
	5.5	(111.6)	(106.1)	5.5	(107.1)	(101.6)
Payments from plan:						
Benefit payments	(150.6)	150.6	-	(149.5)	149.5	_
Administrative costs	(2.2)	2.2	-	(1.7)	1.7	-
MEPS DC bulk transfer**	(3.0)	4.0	1.0			
	(155.8)	156.8	1.0	(151.2)	151.2	-
Liability/(asset) at 31 March	3,263.4	(3,580.2)	(316.8)	3,523.3	(3,584.6)	(61.3)

<sup>\*\*</sup>During the year the MEPS DC section of the scheme has been transferred into WPD's defined contribution scheme.

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# 27. Retirement benefit obligations (continued)

WPUPS	Year ended 31 March 2020			Year ended 31 March 2019		
	Present	Fair value		Present	Fair value	
	value of	of plan		value of	of plan	
	obligation	assets	Total	obligation	assets	Total
	£m	£m	£m	£m	£m	£m
Liability/(asset) at 1 April	525.4	(623.3)	(97.9)	530.3	(604.5)	(74.2)
Administrative costs	0.6	-	0.6	0.4	-	0.4
Interest expense/(income)	12.1	(14.4)	(2.3)	13.3	(15.2)	(1.9)
Past service cost and gains and losses						
on settlement	-	-	-	4.2	-	4.2
	12.7	(14.4)	(1.7)	17.9	(15.2)	2.7
Remeasurements:						
Return on plan assets excluding amounts						
included in interest income	-	(13.5)	(13.5)	-	(33.6)	(33.6)
Loss/(gain) from change in						
demographic assumptions	5.4	-	5.4	(18.6)	-	(18.6)
(Gain)/loss from change in						
financial assumptions	(22.6)	-	(22.6)	26.6	-	26.6
Experience gains	(19.1)	-	(19.1)	(0.8)	-	(0.8)
	(36.3)	(13.5)	(49.8)	7.2	(33.6)	(26.4)
Contributions:						
Employers	-	-	-	-	-	_
1 7	-	-	-	-	-	_
Payments from plan:						
Benefit payments	(25.1)	25.1	-	(29.6)	29.6	_
Administrative costs	(0.6)	0.6	-	(0.4)	0.4	_
	(25.7)	25.7	-	(30.0)	30.0	-
	486.1	((25.5)	(140.4)	505.4	(622.2)	(07.0)
Liability/(asset) at 31 March	476.1	(625.5)	(149.4)	525.4	(623.3)	(97.9)

For the year ended 31 March 2020

# 27. Retirement benefit obligations (continued)

Infralec 92	Year o	ended 31 Mar	ch 2020	Year e	ended 31 Marcl	n 2019
	Present	Fair value		Present	Fair value	
	value of	of plan		value of	of plan	
	obligation	assets	Total	obligation	assets	Total
	£m	£m	£m	£m	£m	£m
Liability/(asset) at 1 April	13.3	(15.9)	(2.6)	13.1	(15.3)	(2.2)
Interest expense/(income)	0.3	(0.4)	(0.1)	0.3	(0.4)	(0.1)
Past service cost and gains and losses						
on settlement	-	-	-	0.2	-	0.2
	0.3	(0.4)	(0.1)	0.5	(0.4)	0.1
Remeasurements:						
Return on plan assets excluding amounts						
included in interest income	_	0.7	0.7	_	(0.8)	(0.8)
Gain from change in	_	0.7	0.7		(0.0)	(0.0)
demographic assumptions	_	_	_	(0.5)	_	(0.5)
(Gain)/loss from change in				(0.5)		(0.5)
financial assumptions	(0.6)	_	(0.6)	0.7	_	0.7
Experience losses	0.1	_	0.1	0.1	_	0.1
	(0.5)	0.7	0.2	0.3	(0.8)	(0.5)
Contributions:						
Employers	<u> </u>	<u> </u>	-	-	<u>-</u>	<u>-</u>
Payments from plan:	(O. =)			(0.3)		
Benefit payments	(0.5)	0.5	-	(0.6)	0.6	
	(0.5)	0.5	-	(0.6)	0.6	
Liability/(asset) at 31 March	12.6	(15.1)	(2.5)	13.3	(15.9)	(2.6)
The significant actuarial assumptions made w	rara as fallouss			20	20	
The significant actuarial assumptions made w	ere as follows.		ESPS WPD	ESPS CN	WPUPS	Infralec 92
			%	%	%	%
RPI Inflation			2.60	2.60	2.60	2.60
CPI Inflation			2.00	2.00	2.00	2.00
Rate of general long-term salary increases			3.10	3.10	N/a	N/a
RPI-linked pension increases			2.60	2.60	2.60	2.60
CPI-linked pension increases			N/a	N/a	2.00	N/a
Post-88 GMP pension increases			1.85	1.85	1.85	1.85
Discount rate for scheme liabilities			2.31	2.31	2.31	2.31

For the year ended 31 March 2020

## 27. Retirement benefit obligations (continued)

The significant actuarial assumptions made were as follows:	2019				
	ESPS WPD	ESPS CN	WPUPS	Infralec 92	
	%	%	%	%	
RPI Inflation	3.15	3.15	3.15	3.15	
CPI Inflation	2.05	2.05	2.05	2.05	
Rate of general long-term salary increases	3.65	3.65	N/a	N/a	
RPI-linked pension increases	3.10	3.10	3.15	3.15	
CPI-linked pension increases	N/a	N/a	2.05	N/a	
Post-88 GMP pension increases	1.90	1.90	1.90	1.90	
Discount rate for scheme liabilities	2.36	2.36	2.36	2.36	

Assumptions relating to future mortality are set based on actuarial advice in accordance with published statistics and experience. The impact of the COVID-19 outbreak on long term mortality trends is currently unclear and therefore has not been included in the mortality assumptions. These assumptions translate into an average life expectancy in years for a member at age 60:

## ESPS WPD

	31 March 2020	31 March 2019
Mortality table adopted	Based on S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate	Based on S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate
Life expectancy for a male currently aged 60	25.9	25.8
Life expectancy for a female currently aged 60	27.9	27.9
Life expectancy at 60 for a male currently aged 40	26.7	27.0
Life expectancy at 60 for a female currently aged 40	28.8	29.1

# ESPS CN

·	31 March 2020	31 March 2019
Mortality table adopted	Based on S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate	Based on S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate
Life expectancy for a male currently aged 60	25.9	25.8
Life expectancy for a female currently aged 60	27.9	27.9
Life expectancy at 60 for a male currently aged 40	26.7	26.6
Life expectancy at 60 for a female currently aged 40	28.8	28.8

For the year ended 31 March 2020

## 27. Retirement benefit obligations (continued)

## **WPUPS**

	31 March 2020	31 March 2019
Mortality table adopted	*with CMI 2018 core projections and a 1.0% per annum long-term improvement rate	Pensions <£25,500 pa at 31/03/16: 111% (else 78%) of S2NXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate
Life expectancy for a male currently aged 60	26.0	25.3
Life expectancy for a female currently aged 60	28.4	27.9
Life expectancy at 60 for a male currently aged 40	27.0	26.4
Life expectancy at 60 for a female currently aged 40	29.6	28.7

<sup>\*</sup> Male non-pensioners: 105% of S3PMA base tables, female non-pensioners: 97% of S3PFA\_middle base tables, male pensioners 103% of S3PMA base tables, female pensioners: 96% of S3PFA\_middle base tables

Infralec 92

	31 March 2020	31 March 2019
Mortality table adopted	100% of S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate	100% of S2PXA base tables with CMI 2018 core projections and a 1.0% per annum long-term improvement rate
Life expectancy for a male currently aged 60	25.9	25.8
Life expectancy for a female currently aged 60	27.9	27.9
Life expectancy at 60 for a male currently aged 40	27.1	27.0
Life expectancy at 60 for a female currently aged 40	29.2	29.1

The sensitivity of the defined benefit obligation to changes in the principal assumptions is:

	Impact on defined benefit obligat				tion	
	Change in assumption %	ESPS WPD £m	ESPS CN £m	WPUPS £m	Infralec 92 £m	
Discount rate	-/+0.50%	+206.6/-184.6 +	-276.8/-249.3	+32.6/-29.9	+0.9/-0.8	
RPI Inflation	+/-0.50%	+196.3/-165.7 +	259.1/-220.0	+27.9/-23.7	+0.7/-0.7	
Life expectancy	+ 1 year	103.2	145.1	20.7	0.6	

The above sensitivity analysis on the discount rate is based on a change in assumption while holding all other assumptions constant. The change in RPI inflation assumption impacts on the CPI assumption, revaluation in deferment and pension increase assumptions. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as when calculating the pension liability recognised within the balance sheet.

For the year ended 31 March 2020

## 27. Retirement benefit obligations (continued)

ESPS WPD scheme assets are comprised as follows:	31 Mai	rch 2020	31 Mar	ch 2019
ESTS WTD seneme assets are comprised as follows:		Of which	011.141	Of which
		not quoted		not quoted
		in an active		in an active
	Total	market	Total	market
	£m	£m	£m	£m
Equities	486.0	_	532.3	_
Property (i)	160.9	160.9	166.9	166.9
Macro-orientated	109.2	100.5	288.3	100.9
Multi strategy	601.1	-	496.5	_
LDI strategy	1,053.0	-	935.1	_
Other including cash and net current assets	4.5	-	3.4	_
Total	2,414.7	160.9	2,422.5	166.9
ESPS CN scheme assets are comprised as follows:	31 Mar	rch 2020	31 Mar	rch 2019
		Of which		Of which
		not quoted		not quoted
	m 4 1	in an active	TD 4.1	in an active
	Total	market	Total	market
	£m	£m	£m	£m
Equities	590.5	-	662.6	-
Credit	89.2	-	101.7	-
Property (i)	119.3	119.3	125.8	125.8
Macro-orientated	217.7	217.7	383.6	383.6
Multi strategy	794.6	-	679.8	-
LDI strategy	1,646.8	-	1,526.8	-
Other including cash and net current assets	122.1	-	104.3	-
Total	3,580.2	337.0	3,584.6	509.4
WPUPS scheme assets are comprised as follows:	31 May	rch 2020	31 Mar	ch 2019
wi of 5 scheme assets are comprised as follows.		Of which	J1 Wiai	Of which
		not quoted		not quoted
		in an active		in an active
	Total	market	Total	market
	£m	£m	£m	£m
	<b>50.4</b>			
Equities	72.4 552.2	-	226.5 395.6	-
Government bonds Other	0.9	-	393.6	-
Total	625.5	<u> </u>	623.3	<u>-</u>
		1 2020		1 2010
Infralec 92 scheme assets are comprised as follows:	31 Mai	of which	31 Mai	och 2019 Of which
		not quoted		not quoted
		in an active		in an active
	Total	market	Total	market
	£m	£m	£m	£m
Partition				
Equities	5.4	-	6.4	-
Government bonds	5.7	-	5.6	-
Corporate bonds	3.8	-	3.7	-
Other	0.2	-	0.1	-

<sup>(</sup>i) Due to the COVID-19 outbreak, there is some uncertainty in respect of property valuations and fair values by independent valuers, in line with current market practice, have been reported on the basis of "material valuation uncertainty" (refer to note 14 for details). However, as is evident in the table above, property assets represent a small fraction of total scheme assets and the aggregate surplus of the defined benefit plan is sufficient to cover the loss, if any, on the long term value of property assets. The sensitivity of the fair value of plan assets to a change in the valuation of property assets is as follows:

15.1

15.8

**Total** 

For the year ended 31 March 2020

### 27. Retirement benefit obligations (continued)

		Impa	ct on defined be	nefit obligation	on
	Change in assumption %	ESPS WPD £m	ESPS CN £m	WPUPS £m	Infralec 92 £m
Fair value of property assets	- 10 %	(16.1)	(24.1)	_	-
Fair value of property assets	- 15 %	(24.1)	(36.2)	-	-

There is no self-investment in any of the schemes.

Through its defined benefit pension plans, the WPD Group is exposed to a number of risks, the most significant of which are detailed below:

Asset volatility	The liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The scheme holds a significant proportion of growth assets (e.g. equities) which are expected to outperform corporate bonds in the long-term while providing volatility and risk in the short-term. The allocation to growth assets is monitored such that it is suitable with the schemes' long-term objectives.
Changes in bond yields	A decrease in corporate bond yields will increase the schemes' liabilities, although this will be partially offset by an increase in the value of the schemes' bond holdings.
Inflation risk	The majority of the schemes' benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). The majority of the assets are either unaffected by or loosely correlated with inflation, meaning than an increase in inflation will increase the deficit.
Life expectancy	The majority of the schemes' obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

The schemes use government bonds, corporate bonds and cash as matching assets. The remainder of assets are used as growth assets.

The employer has agreed that it will aim to eliminate the actuarial deficits (as assessed on the ongoing funding basis) by 30 November 2024 for the WPD segment of the ESPS, by 31 July 2024 for the CN segment of the ESPS, and by 30 September 2024 for I92.

The current agreed employer contributions for the WPD segment of the ESPS are 31.2% per annum of pensionable salaries from 1 April 2020 to 31 March 2023 and 42.4% per annum of pensionable salaries thereafter in respect of future benefit accruals, expenses (including PPF levies) and death in service benefits plus an additional £1.8m per annum in respect of expenses. Company deficit contributions are £80.0m per annum payable from 1 April 2020 to 31 March 2021 and £18.0m per annum payable from 1 April 2021 to 30 November 2024.

The current agreed employer contributions for the CN segment of the ESPS are 27.9% per annum of pensionable salaries from 1 April 2020 to 31 March 2023 and 37.0% per annum of pensionable salaries thereafter in respect of future benefit accrual, expenses (including PPF levies) and death in service benefits plus an additional £1.8m per annum in respect of expenses. Company deficit contributions are £80.0m per annum payable from 1 April 2020 to 31 March 2021 and £36.0m per annum payable from 1 April 2021 to 31 July 2024.

The results of the 31 March 2019 funding valuation showed that WPUPS was in surplus on the ongoing funding basis. As a result, no deficit contributions are required, and the expected employer contributions to the scheme for the year ending 31 March 2021 are nil.

The current agreed employer contribution to Infralec 92 is that on 31 March each year, from 31 March 2021 to 31 March 2024 (inclusive) WPD will pay £0.235m per annum.

Funding levels are monitored on a regular basis and the next triennial valuation is due to be completed as at 31 March 2022.

Current expected total employer contributions for the year ending 31 March 2021 are £103.7m for the WPD segment of the ESPS and £104.9m for the CN segment of the ESPS.

Please note the results of the actuarial funding valuation as at 31 March 2022 may give rise to a revised schedule of contributions and as such the quantities in the paragraph above may be liable to change.

The weighted average duration of the defined benefit obligation is around 17 years for the WPD segment of the ESPS, 16 years for the CN segment of the ESPS, and around 13 years for WPUPS and Infralec 92.

For the year ended 31 March 2020

### 28. Provisions

	WPUPS	Asset				
	Reimbursement Agreement (i)	Retirement Obligations (ii)	Insurance (iii)	Pensions (iv)	Other (v)	Total
-	£m	£m	£m	£m	£m	£m
At 1 April 2019	97.9	37.6	18.3	4.2	3.3	161.3
Charged to income statement:						
Additional provisions	1.7	8.4	(0.8)	0.1	0.3	9.7
WPUPS reimbursement remeasurements	49.8	-	-	-	-	49.8
Utilised during year		(1.4)		(0.7)	(0.3)	(2.4)
At 31 March 2020	149.4	44.6	17.5	3.6	3.3	218.4
Provisions have been analysed between o	current and non-cur	rent as follows:				
Current	_	1.4	5.8	0.7	2.5	10.4
Non-current	149.4	43.2	11.7	2.9	0.8	208.0
At 31 March 2020	149.4	44.6	17.5	3.6	3.3	218.4
Current	-	1.2	6.7	0.6	2.5	11.0
Non-current	97.9	36.4	11.6	3.6	0.8	150.3
At 31 March 2019	97.9	37.6	18.3	4.2	3.3	161.3

- (i) WPD South Wales is the principal employer for WPUPS, which is a defined benefit scheme providing benefits relating to previous employees of an affiliate group which was previously headed by Hyder plc (now Hyder Limited in liquidation). WPD South Wales will fund the actuarial deficit. However, as PPL WPD Limited, the Company's parent, has taken full financial responsibility for this scheme, WPD South Wales will be reimbursed for these payments. As PPL WPD Limited is outside the WPD Group, the value of the reimbursement agreement is stated in the balance sheet as a provision above, and matches the gross asset recorded under IAS 19 (Note 27).
- (ii) Asset retirement obligations relate to an estimate of the costs of dismantling and removing wood poles and fluid filled cables at the end of their useful lives and are expected to be settled over the next seventy years. Wood poles and fluid filled cables are included in distribution network within property, plant and equipment.
- (iii) Insurance provisions relate to claims covered by the WPD Group's wholly-owned captive insurance company, Aztec Insurance Limited ("Aztec"), based in Guernsey, and claims covered by external insurers. This includes third party motor claims, employers' liability, public and product liability, and professional indemnity and includes claims that are reported but not yet paid and anticipated cost of claims incurred but not yet reported. The directors expect the provision to be settled in the next five years.
- (iv) Pension provisions relate to expected settlements of liabilities relating to the pension liability relating to the Electricity Association Technology Limited ("EATL") and are expected to be settled over a period of approximately nine years.
- (v) Other provisions relate principally to onerous property contracts, uninsured losses, and miscellaneous claims arising in the ordinary course of business; the directors expect other provisions to be settled within the next two years.

## 29. Called-up share capital

	2020 £m	2019 £m
<b>Allotted, called-up and fully paid</b> 1,657,592,372 (2019: 1,657,592,372) ordinary shares of £1 each	1,657.6	1,657.6

The shares entitle the holders thereof to one vote per share held. Each share ranks equally for any dividend declared and any distribution made on a winding up. The shares are not redeemable.

For the year ended 31 March 2020

## 30. Capital and reserves

	2020 £m	2019 £m
Share capital	1,657.6	1,657.6
Merger reserve	(963.1)	(963.1)
Hedging reserve	1.2	(5.2)
Retained earnings	4,590.1	4,023.4
	5,285.8	4,712.7

The **share capital** represents the nominal value of the authorised ordinary shares in the Company in issue which carry a right to participate in the distribution of dividends or capital of the Company.

The merger reserve arose on the restructuring of WPD Group entities under common control in October 2014 and September 2001.

The **hedging reserve** comprises the effective portion of the cumulative net change in the fair value of cash flow hedge derivative instruments related to hedged transactions that have not yet occurred.

### 31. Contingent liabilities

### Legal proceedings

The WPD Group's businesses are parties to various legal claims, actions and complaints. Although the WPD Group is unable to predict with certainty whether or not it will ultimately be successful in these legal proceedings or, if not, what the impact might be, the directors currently believe that disposition of these matters will not have a materially adverse effect on the WPD Group's financial statements.

#### 32. Commitments

### Capital commitments

Capital expenditure contracted for at the balance sheet date but not recognised in the financial statements is as follows:

	2020	2019
	£m	£m
Property, plant and equipment	51.9	35.1

Operating lease commitments - WPD Group as lessor

The WPD Group has entered into commercial property leases on its investment property portfolio, consisting of the WPD Group's surplus offices, shops remaining from a discontinued business, and surplus land, and also on its fibres. The leases have lease terms between 1 and 125 years, and have various terms, escalation clauses and renewable rights. Leases include a clause to enable upward revision of rental charge on a review cycle set on lease inception according to prevailing market conditions.

Future minimum rentals receivable under non-cancellable operating leases at 31 March are as follows:

	2020 £m	2019 £m
Year 1	4.5	3.3
Year 2	3.6	3.1
Year 3	3.2	2.5
Year 4	2.9	2.3
Year 5	2.4	2.0
Year 6 and onwards	9.4	9.1
	26.0	22.3

## Notes to the Western Power Distribution plc consolidated financial statements (continued)

For the year ended 31 March 2020

# 32. Commitments (continued)

Guarantees and indemnities

The WPD Group has provided guarantees in respect of the funding required by the WPD Group's pension schemes.

### 33. Related party transactions

The immediate parent undertaking of the WPD Group is PPL WPD Investments Limited, which is registered in England and Wales.

The smallest and largest group in which the results of the Company are consolidated is that headed by PPL Corporation incorporated in the United States of America, which is the ultimate parent undertaking and controlling party. Copies of its accounts may be obtained from its registered address at Two North Ninth Street, Allentown, Pennsylvania, PA18101-1179, US.

There are no personnel, other than the directors, who as key management have authority and responsibility for planning, directing and controlling the activities, directly or indirectly, of the WPD Group. Details of directors' compensation are set out in Note 9.

#### Loan to PPL affiliate

In February 2011, the WPD Group purchased \$200m nominal at a premium of \$21m from a PPL affiliate, PMDC Chile, of the \$400M 2018 6.42% USD denominated Eurobond issued by PPL UK Resources Limited. This was funded through the repayment of a loan from an affiliate and the issue of share capital. In May 2017, the maturity date was extended to 2021.

The investment has the following terms and conditions:

Name of PPL affiliate	<b>Amount of investment</b>	<u>Term</u>	<u>Interest rate</u>
PPL UK Resources Ltd	\$200m	Repayable on 31 July 2021	6.42%

The WPD Group recorded interest receivable of £10.1m (2019: £9.2m) on the investment.

#### WPUPS reimbursement agreement

WPD South Wales is the principal employer for WPUPS, which is a defined benefit scheme providing benefits relating to previous employees of an affiliate group which was previously headed by Hyder plc (now Hyder Limited in liquidation). WPD South Wales will fund the actuarial deficit. However, PPL WPD Limited, the Company's parent, has taken full financial responsibility for this scheme, WPD South Wales will be reimbursed for these payments. As PPL WPD Limited is outside the WPD Group, the value of the reimbursement agreement is stated in the balance sheet (Note 28) and matches the gross asset/liability recorded under IAS 19 (Note 27)

## 34. Events after the reporting period

On 15 June 2020, the Company paid an interim dividend of £30.0m to PPL WPD Investments Limited.

On 7 April 2020, the share capital of the Company was reduced by £600m. The share capital reduction was approved by the directors on 28 February 2020.

Subsequent to the year end, the COVID-19 situation continues to unfold. We have outlined our detailed response to COVID-19 and the impacts of COVID-19 on the Group in the Strategic report. The impact of COVID-19 on our liquidity and going concern have been discussed in detail in the Directors' report.

In June 2020, in response to the cash flow implications of COVID-19 on electricity suppliers, Ofgem, in conjunction with the Energy Networks Association ("ENA"), developed a payment deferral scheme in order to provide relief to cash flow constrained suppliers. The scheme is limited to suppliers without an investment grade credit rating, i.e. those suppliers that have fewer alternative options for securing financing, and is considered as a last resort option should other financing routes be unavailable. Under the scheme, suppliers can request an extended period for payment of monthly network charges without any additional security. The deferred payments would accrue interest at the default rates set out in the relevant industry codes and will be required to be repaid by 31 March 2021 and prior to any payment of dividends or executive bonuses by the suppliers. WPD does not anticipate this deferral scheme to have a material impact on the Group's ECL. The impact, if any, would pertain to the timing of cash receipts over the next 12 months and has been taken into consideration in determining going concern.

# Parent Company financial statements of Western Power Distribution plc Company balance sheet

As at 31 March 2020

		2020	2019
	Note	£m	£m
Non-current assets			
Investments:			
Shares in subsidiary undertakings	4	2,876.0	2,876.0
Loans to group undertakings	4	162.2	155.5
Derivative financial instruments		156.0	97.4
		3,194.2	3,128.9
Current assets			
Derivative financial instruments		7.1	5.5
Debtors	5	617.4	396.8
Cash at bank		10.3	28.4
		634.8	430.7
Creditors - amounts falling due within one year	6	(188.0)	(179.8)
Net current assets		446.8	250.9
Total assets less current liabilities		3,641.0	3,379.8
Creditors - amounts falling due after more than one year	6	(1,525.7)	(1,453.8)
Provision for liabilities			
Deferred tax	7	(4.6)	-
Net assets		2,110.7	1,926.0
Capital and reserves		4 / 8 8 /	
Called-up share capital	8	1,657.6	1,657.6
Hedging reserve	9	452.1	(0.5)
Profit and loss account		453.1	268.9
Equity shareholders' funds		2,110.7	1,926.0

The Company reported a profit for the financial year ended 31 March 2020 of £384.3m (2019: £19.6m loss) and other comprehensive income of £0.5m (2019: £3.5m).

The financial statements of the Company on pages 108 to 118 were approved by the Board of Directors and authorised for issue on 23 July 2020 and signed on its behalf by:

P Swift Chief Executive I R Williams Finance Director

# **Company statement of changes in equity** For the year ended 31 March 2020

Tor the year chiefe 31 March 2020	Share capital £m	Hedging reserve £m	Retained earnings £m	Total equity £m
At 1 April 2018	1,657.6	(4.0)	588.7	2,242.3
Loss for the year	-	-	(19.6)	(19.6)
Other comprehensive income		3.5	-	3.5
Total comprehensive income/(loss) for the year	-	3.5	(19.6)	(16.1)
Equity dividends paid	-	-	(300.2)	(300.2)
At 31 March 2019	1,657.6	(0.5)	268.9	1,926.0
Profit for the year	-	-	384.3	384.3
Other comprehensive income	-	0.5	-	0.5
Total comprehensive income for the year	-	0.5	384.3	384.8
Equity dividends paid	<u>-</u>		(200.1)	(200.1)
At 31 March 2020	1,657.6	-	453.1	2,110.7

## Notes to the Company financial statements

For the year ended 31 March 2020

# 1. Authorisation of financial statements and statement of compliance with FRS 101

The parent Company financial statements of Western Power Distribution plc (the "Company") for the year ended 31 March 2020 were authorised for issue by the board of directors on 23 July 2020 and the balance sheet was signed on the board's behalf by P Swift and I R Williams. Western Power Distribution plc is a public limited company incorporated and registered in England and Wales.

The Company meets the definition of a qualifying entity under FRS 100 "Application of Financial Reporting Requirements". These financial statements were prepared in accordance with Financial Reporting Standard 101 "Reduced Disclosure Framework" ("FRS 101") and in accordance with applicable accounting standards.

# 2. Significant accounting policies

#### Basis of preparation

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to financial instruments, capital management, presentation of comparative information in respect of certain assets, presentation of a cash flow statement, standards not yet effective, impairment of assets and related party transactions. Where required, equivalent disclosures are given in the group accounts of Western Power Distribution plc which are included on pages to 1 to 107.

As permitted by Section 408 of the Companies Act 2006 the Company has elected not to present its own income statement or statement of comprehensive income for the year. The profit attributable to the Company is disclosed in the footnote to the Company's balance sheet.

The financial statements have been prepared on the historical cost basis, except for the revaluation of derivative financial instruments that are measured at fair value, as explained in the accounting policies below. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or liability, the Company takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2, leasing transactions that are within the scope of IFRS 16, and measurements that have some similarities to fair value but are not fair value such as net realisable value in IAS 2 or value in use in IAS 36.

The Company's financial statements are presented in Sterling as this is the currency of the primary economic environment in which the Company operates. All values are rounded to the nearest hundred thousand pounds except when otherwise indicated.

The principal accounting policies adopted are set out below.

### Going concern

The directors have prepared the financial statements on the going concern basis as they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. The current financial position of the Company shows net current assets of £446.8m. Having assessed the Company's investment portfolio, its consistent dividend inflow and the ability to raise finance externally as well as internally through WPD Group undertakings, the directors have concluded that the going concern basis of preparation remains appropriate.

The impacts of COVID-19 have also been taken into consideration in arriving at the going concern assumption for preparation of the financial statements. Since the Company's income is primarily dividend and interest income from WPD Group entities, the Company does not consider that at this stage there is a material uncertainty casting a doubt over the entity's ability to continue as a going concern. The WPD Group's operating companies are regulated DNOs. DNOs are essential in keeping critical infrastructure assets operating safely and securely and in making sure that homes and businesses across the licensed regions have continued access to electricity supplies. Therefore, even in these challenging times, whereby many business sectors are impacted severely, the operating companies within the WPD Group have a continuing licence obligation to be a sustainable business and provide essential services to society. Based on licence conditions and price control allowances, the Company is expected to have a continuing, stable stream of revenue.

For further details of the impact of COVID-19 on the WPD Group refer to the Strategic report (page 18).

For the year ended 31 March 2020

# 2. Significant accounting policies (continued)

# Impact of new International Financial Reporting Standards

The following new standards are effective for accounting periods beginning on or after 1 January 2019:

#### IFRS 16

IFRS 16 "Leases" supersedes the previous lease guidance including IAS 17 "Leases" and the related interpretations and is effective for accounting periods beginning on or after 1 January 2019. IFRS 16 provides comprehensive guidance for the identification of lease arrangements for both lessee and lessor and a new model for lessee accounting in which all leases, other than short-term and small-ticket-item leases, are accounted for by the recognition on the balance sheet of a right-to-use asset and a lease liability, and the subsequent amortisation of the right-to-use asset and unwinding of lease liability using an appropriate discount rate over the lease term.

The Company has assessed the impact of this standard and concluded that there was no material change to the Company's financial statements.

#### IFRIC 23

IFRIC 23 "Uncertainty over Income Tax Treatments" is effective for annual periods beginning on or after 1 January 2019 and aims to clarify the accounting for uncertainties in income taxes. IFRIC 23 is to be applied to the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, when there is uncertainty over income tax treatments under IAS 12 "Income Taxes".

The Company has assessed the impact of this standard and concluded that there was no material change to the Company's financial statements.

#### Foreign currencies

Transactions in foreign currencies are initially recorded in the entity's functional currency by applying the spot exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to profit and loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

#### Taxation

Current tax is measured at the amount expected to be payable (or recoverable) in respect of the taxable profit (or loss) for the period based on tax rates and laws that have been enacted or substantively enacted at the balance sheet date. This includes UK corporation tax payable to HM Revenue & Customs ("HMRC") and amounts payable to (or receivable from) other UK group companies for losses and other amounts transferred between them ("group relief").

Deferred tax is the tax expected to be payable (or recoverable) in future periods due to differences between the time when profits and losses are recognised in the financial statements and the time when those profits and losses are included in tax returns filed with HMRC. These temporary differences arise in the current period and then reverse in future periods. The temporary differences are calculated by comparing the carrying value of assets and liabilities at the balance sheet date with their corresponding tax bases included in tax returns.

Deferred tax is recognised on all temporary differences except:

- where the temporary difference arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss;
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future; and
- deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the asset may be recovered.

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods when the temporary differences will reverse based on tax rates and laws that have been enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are offset only to the extent permitted by tax legislation.

For the year ended 31 March 2020

## 2. Significant accounting policies (continued)

#### Taxation (continued)

Income tax is charged or credited to other comprehensive income if it relates to items that are charged or credited to other comprehensive income. Similarly, income tax is charged or credited directly to equity if it relates to items that are credited or charged directly to equity. Otherwise income tax is recognised in profit and loss.

#### Financial assets

Financial assets are classified as debt instruments at amortised cost; debt instruments at fair value through other comprehensive income ("FVOCI"); financial assets at fair value through profit and loss ("FVTPL"); derivatives designated as hedging instruments in an effective hedge; or as equity instruments designated at FVOCI, as appropriate. Financial assets include cash at bank, debtors, investments, and derivative financial instruments.. The Company determines the classification of its financial assets at initial recognition. Financial assets are recognised initially at fair value, normally being the transaction price plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs. For financial assets at FVTPL, transaction costs are immediately recognised in profit and loss.

The subsequent measurement of financial assets depends on their classification, as follows:

#### Debt instruments at amortised cost

Debt instruments that meet the hold-to-collect business model test and sole payment principal and interest ("SPPI") contractual cash flow test, are carried at amortised cost using the effective interest method, if the time value of money is significant. Gains and losses are recognised in income when the debt instruments are derecognised or impaired, as well as through the amortisation process. This category of financial assets includes cash at bank, debtors and investments.

#### Financial assets at FVOCI

Financial assets at FVOCI, that meet the sole payment principal and interest ("SPPI") contractual cash flow test and the objective of the Group is achieved both by collecting contractual cash flows and selling financial assets, are carried on the balance sheet at fair value with gains or losses recognised in other comprehensive income. This category of financial assets include derivatives designated as hedging instruments in an effective cash flow hedge.

# Derivatives designated as hedging instruments in an effective hedge

These derivatives are carried on the balance sheet at fair value. The treatment of gains and losses arising from revaluation is described below in the accounting policy for derivative financial instruments and hedging activities.

# Impairment of financial assets

The Company recognises impairment on financial assets following the expected credit loss ("ECL") model in IFRS 9.

#### Debtors

Debtors mainly comprise amounts owed by group undertakings and are considered to be low risk. Therefore the impairment provision is determined as 12 months expected credit loss. The 12-month ECL results from those default events on the financial assets that are possible within 12 months after the reporting date.

#### Investments

Investments are considered to be low risk, and therefore the impairment provision is determined as 12-month expected credit loss. The 12-month ECL results from those default events on the financial assets that are possible within 12 months after the reporting date.

## Cash at bank and in hand

Cash at bank is subject to the impairment requirements of IFRS 9 but the impairment loss on these is deemed immaterial since they have an insignificant risk of change in value.

# Financial liabilities

Financial liabilities are classified as financial liabilities at FVTPL; or as financial liabilities measured at amortised cost, as appropriate. Financial liabilities include creditors. The Company determines the classification of its financial liabilities at initial recognition. The measurement of financial liabilities depends on their classification, as follows:

## Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss are carried on the balance sheet at fair value with gains or losses recognised in the income statement. Derivatives, other than those designated as effective hedging instruments, are included in this category.

For the year ended 31 March 2020

## 2. Significant accounting policies (continued)

## Financial liabilities (continued)

Financial liabilities measured at amortised cost

All other financial liabilities are initially recognised at fair value. For interest-bearing loans and borrowings this is the fair value of the proceeds received net of issue costs associated with the borrowing.

After initial recognition, other financial liabilities are subsequently measured at amortised cost. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in interest and other income and finance costs.

This category of financial liabilities includes creditors.

#### Derivative financial instruments and hedging

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

Gains or losses arising from changes in the fair value of derivatives that are not designated as effective hedging instruments are recognised in the income statement.

## Offsetting of financial assets and liabilities

Financial assets and liabilities are presented gross in the balance sheet unless both of the following criteria are met: the Company currently has a legally enforceable right to set off the recognised amounts; and the Company intends to either settle on a net basis or realise the asset and settle the liability simultaneously. A right of set off is the Company's legal right to settle an amount payable to a creditor by applying against it an amount receivable from the same counterparty. The relevant legal jurisdiction and laws applicable to the relationships between the parties are considered when assessing whether a current legally enforceable right to set off exists.

#### Dividends

Dividend distributions are recognised in the period in which the dividends are paid.

#### Share capital

Ordinary shares are classified as equity and are recorded at the par value of proceeds received, net of direct issue costs. Where shares are issued above par value, the proceeds in excess of par value are recorded in the share premium account.

## Merger reserve

A merger reserve is recorded as a result of the application of the pooling of interests basis of consolidation for the reorganisation of entities under common control a merger reserves has been recorded.

#### 3. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Company's accounting policies, which are described in Note 2, 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 period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

# Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting period that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

For the year ended 31 March 2020

# 3. Critical accounting judgements and key sources of estimation uncertainty (continued)

# Key sources of estimation uncertainty (continued)

#### Financial instruments

Certain financial instruments are carried on the balance sheet at fair value. Fair values are estimated by reference, in part, to published price quotations and in part by using valuation techniques.

There are no judgements dependent upon assumptions which could change in the next financial year and have a material effect on the carrying amounts of assets and liabilities recognised at the balance sheet date.

4. Investments	Subsidiary undertakings £m	Parent Company debt £m	Total £m
Cost			
At 1 April 2019	2,876.0	155.5	3,031.5
Amortisation of premium	-	(0.9)	(0.9)
Exchange rate movement	-	7.7	7.7
At 31 March 2020	2,876.0	162.3	3,038.3
Provision for impairment (ECL)	-	(0.1)	(0.1)
Net book value at 31 March 2020	2,876.0	162.2	3,038.2

Details of the Company's subsidiary undertakings are as follows:

Subsidiary undertakings	Principal activity	Proportion
		%
Western Power Distribution (South West) plc	Electricity distribution	100
Western Power Distribution (South Wales) plc	Electricity distribution	100
Western Power Distribution (East Midlands) plc	Electricity distribution	100
Western Power Distribution (West Midlands) plc	Electricity distribution	100
WPD Investment Holdings Limited	Investment company	100
WPD Distribution Network Holdings Limited	Investment company	100
PPL Island Limited	Investment company	100
PPL WEM Limited	Investment company	100
PPL Midlands Limited	Investment company	100
PPL UK Investments Limited	Investment company	100
Western Power Distribution Investments Limited	Investment company	100
WPD Telecoms Limited	Telecommunications	100
Western Power Generation Limited	Power generation	100
WPD Property Investments Limited	Property management	100
Kelston Properties 2 Limited	Property management	100
Aztec Insurance Limited ^	Insurance	100
South Western Helicopters Limited	Helicopter operator	100
WPD Smart Metering Limited	Electricity Metering	100
WPD Midlands Properties Limited (in liquidation)	Investment company	100
WPD Limited ^	Property management	100
Hyder Profit Sharing Trustees Limited	Dormant company	100
WW Share Scheme Trustees Limited	Dormant company	100
South Wales Electricity Share Scheme Trustees Limited	Dormant company	100
Infralec 1992 Pension Trustee Limited	Dormant company	100
WPD Midlands Networks Contracting Limited	Dormant company	100
Central Networks Trustees Limited	Dormant company	100
WPD Share Scheme Trustees Limited	Dormant company	100
Western Power Pension Trustee Limited	Dormant company	100

For the year ended 31 March 2020

# 4. Investments (continued)

Subsidiary undertakings	Principal activity	Proportion
WPD Limited	Dormant company	100
Meter Reading Services Limited	Dormant company	100
Meter Operator Services Limited	Dormant company	100

<sup>^</sup> Incorporated in Guernsey.

All undertakings are registered in England and Wales unless stated.

Except for WPD Investment Holdings Limited and PPL UK Investments Limited, which are owned 100% directly, all shares are held by subsidiary undertakings. All holdings are in ordinary shares.

Except for Aztec Insurance Limited and WPD Limited, the registered office of all subsidiary undertakings is Avonbank, Feeder Road, Bristol BS2 0TB. The registered office for Aztec Insurance Limited is Marsh Management Services Limited, PO Box 34, St Martins House, Le Bordage, St Peters Port, Guernsey, GY1 4AU and for WPD Limited is Elizabeth House, Les Ruettes Brayes, St Peters Port, Guernsey, GY1 1EW.

5. Debtors	2020 £m	2019 £m
Amounts falling due within one year:	žIII	ĮIII.
Amounts owed by Group undertakings	614.7	392.6
Other debtors	2.6	2.5
Prepayments and accrued income	0.1	2.3
Deferred tax asset	0.1	1.7
Deferred tax asset	-	1./
	617.4	396.8
Amounts owed by Group undertakings		
	2020	2019
	£m	£m
Inter-company Notes receivable from:		
PPL WEM Limited (1)	238.8	238.8
WPD Distribution Network Holdings Limited (2)	_	147.6
PPL UK Investments Limited (3)	370.0	-
Interest on inter-company Notes receivable from:	2700	
PPL WEM Limited	3.5	3.5
WPD Distribution Network Holdings Limited	-	2.6
PPL UK Investments Limited	2.3	
Inter-company accounts	0.1	0.1
	V	0.1
	614.7	392.6

<sup>(1)</sup> Accrues interest at a fixed rate of 5.0% per annum.

All notes are unsecured and are repayable on demand. The ECL on amounts owed by Group undertakings is £0.1m.

<sup>(2)</sup> Accrues interest at a rate of 1 month libor plus a margin of between 0.9% and 2.0% based on the Company's credit rating.

<sup>(3)</sup> Accrues interest at a rate of 6 month libor plus a margin of 1.25%.

For the year ended 31 March 2020

6. Creditors	2020	2019
	£m	£m
Amounts falling due within one year:		
Syndicated credit facility (1)	161.0	153.4
Amounts owed to Group undertakings	0.9	1.0
Accruals and deferred income	26.1	25.4
	188.0	179.8
	2020	2019
	£m	£m
Amounts falling due after more than one year:		
5.375% US\$500m bonds due 2021 (2)	410.6	398.4
7.375% US\$255m bonds due 2028 (3)	222.1	213.4
3.625% GB£500m bonds due 2023	497.6	496.9
3.5% GB£350m bonds due 2026	345.7	345.1
Term loan facility (4)	49.7	
	1,525.7	1,453.8

Borrowings are stated net of unamortised issue costs of £3.6m (2019: £4.0m), discount on issue of £3.3m (2019: £4.0m) and premium on issue of £24.8m (2019: £32.6m). These costs, together with the interest expense, are allocated to the income statement over the term of the bonds at a constant rate on the carrying amount.

- (1) The amounts borrowed on the Company's £210.0m syndicated credit facility at 31 March 2020 and 31 March 2019 were USD-denominated borrowings of \$200.0m for both periods, which bore interest at 1.77% and 3.32% (interest on the facility accrues at a rate of libor plus a margin of between 1.4% and 2.5% based on the Company's credit rating). At 31 March 2020, the Company had available £49.0m (2019: £56.6m) undrawn in respect of which all conditions precedent had been met. The unused capacity reflects the amount borrowed in GBP of £161.0m (2019: £153.4m) as of the date borrowed.
- (2) The Company is a co-obligor and makes all payments on the \$500m 5.375% notes due 1 May 2021 issued by PPL WEM Limited (the 'WEM Bonds') and has entered into a reimbursement agreement in relation to payments under the WEM Bonds. As a consequence, the Company and WEM are jointly and severally, and fully and unconditionally, liable on the WEM Bonds. Under the terms of a reimbursement agreement, where WEM has given notice of its intention to make payments to the holders of the WEM Bonds, the Company will make payments to WEM equal to such amounts. Having recognised its obligations under the WEM bonds in full, the Company has not recognised any amounts in respect of its obligations under the reimbursement agreement.
- (3) The Company is a co-obligor and makes all payments on the \$255m 7.375% notes due 15 December 2028 issued by PPL UK Distribution Holdings Limited (the "PPLUK Bonds") and has entered into a reimbursement agreement in relation to payments under the PPLUK Bonds. This reimbursement agreement was transferred to PPL UK Resources Limited during the prior year. In accordance with the agreements, the Company and PPL UK Resources Limited are jointly and severally, and fully and unconditionally, liable on the PPLUK Bonds. Under the terms of the reimbursement agreement, where PPL UK Resources Limited has given notice of its intention to make payments to the holders of the PPLUK Bonds, the Company will make payments to PPL UK Resources Limited equal to such amounts. Having recognised its obligations under the PPLUK bonds in full, the Company has not recognised any amounts in respect of its obligations under the reimbursement agreement.
- (4) On 7 June 2019, the Company entered into a £50.0m five year term facility agreement with National Westminster Bank plc. On 13 June 2019, the Company borrowed the full loan amount under the facility. Proceeds of the borrowing were used for general corporate purposes. At 31 March 2020 interest on the facility accrued at a rate of 1.91%, being libor plus a margin of 1.4%.

For the year ended 31 March 2020

## 7. Deferred tax

The following are the deferred tax liabilities and assets recognised by the Company and movements thereon during the current year. All balances relate to temporary differences in respect of non-trade financial transactions.

	2020 £m	2019 £m
Asset at 1 April	(1.7)	(4.9)
Deferred tax charged in the income statement for the period	6.2	2.5
Deferred tax charged in the statement of comprehensive income	0.1	0.7
Liability/(asset) at 31 March	4.6	(1.7)
8. Called-up share capital	2020	2019
	£m	£m
<b>Allotted, called-up and fully paid</b> 1,657,592,372 (2019: 1,657,592,372) ordinary shares of £1 each	1,657.6	1,657.6

The shares entitle the holders thereof to one vote per share held. Each share ranks equally for any dividend declared and any distribution made on a winding up. The shares are not redeemable.

# 9. Hedging reserve

	2020	2019
	£m	£m
At 1 April	(0.5)	(4.0)
Reclassification adjustments for losses on cash flow hedges		
included in profit or loss	0.6	0.9
Fair value of cashed out interest rate swap	-	3.4
Income tax effect	(0.1)	(0.8)
At 31 March	-	(0.5)

The hedging reserve relates to the value received in respect of interest rate derivatives entered into in anticipation of the issue of long-term debt. The effective portion of the loss when the swap was cashed out is being amortised through the income statement over the term of the bond.

## 10. Events after the reporting period

On 7 April 2020, the share capital of the Company was reduced by £600m. The share capital reduction was approved by the directors on 28 February 2020.

On 15 June 2020, the Company paid an interim dividend of £30.0m to PPL WPD Investments Limited.

For the year ended 31 March 2020

## 11. Related party transactions

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

The largest group in which the results of the Company are consolidated is that headed by PPL Corporation incorporated in the United States of America, which is the ultimate parent undertaking and controlling party. Copies of their accounts may be obtained from their registered address at Two North Ninth Street, Allentown, Pennsylvania, PA18101-1179, US.

Investment in PPL affiliate debt

In October 2014, as part of an intra-group reorganisation, WPD acquired \$200m nominal at a premium of \$16m from PPL UK Distribution Holdings Limited of the \$400m 2018 6.42% USD denominated Eurobond issued by PPL UK Resources Limited. During 2018 the maturity date was extended to 2021.

The investment has the following terms and conditions:

Name of PPL affiliate	Amount of investment	<u>Term</u>	Interest rate
PPL UK Resources Ltd	\$200m	Repayable on 31 July 2021	6.42%

The Company recorded interest receivable of £9.2m (2019: £8.9m) on the investment for the period. This includes premium amortisation from when the investment was transferred from a fellow group undertaking in 2014.

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