

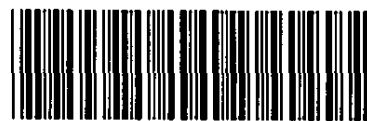
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**Scottish Hydro Electric Power
Distribution plc**

Financial Statements

Year ended 31 March 2012

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Operating and Financial Review

The Operating and Financial Review sets out the main trends and factors underlying the development and performance of the Company during the year ended 31 March 2012, as well as those matters which are likely to affect its future development and performance.

The business, its objectives and strategy

Scottish Hydro Electric Power Distribution plc (the "Company") is a wholly owned subsidiary of SSE plc (the "Group"). The Company distributes electricity to around 746,000 customers in the North of Scotland. It currently has 47,491 kilometres of electricity mains on commission. The Company also provides electricity connections within the Company's licensed area and owns and operates a number of the out of area electricity networks in the rest of Scotland.

The Company is the subject of incentive-based regulation by the industry regulator, the Office of Gas and Electricity Markets (Ofgem), which sets for periods of five years the prices that can be charged for the use of the electricity network, the capital expenditure and the allowed operating expenditure, within a framework known as the Price Control. In broad terms, Ofgem seeks to strike the right balance between attracting investment in electricity networks, encouraging companies to operate the networks as efficiently as possible and ensuring that prices for customers are no higher than they need to be. Ofgem also places specific incentives on companies to improve their efficiency and quality of service.

The Company's strategy and main objectives are to:

- comply fully with all electricity network safety standards and environmental requirements;
- ensure that the electricity network is managed as efficiently as possible, including maintaining tight controls over operational expenditure;
- provide good performance in areas such as reliability of supply, customer service and innovation and thus earn additional incentive-based revenue under the various Ofgem schemes;
- deliver capital expenditure programmes, so that the number and duration of power cuts experienced by customers is kept to a minimum;
- grow the RAV of the networks business and so secure increased revenue; and
- engage constructively with the regulator, Ofgem.

Business performance overview

Performance during 2011/12 has been encouraging and against a range of measures has continued to be good. The following financial and operational key performance indicators are used by the Company in measuring performance:

a) Operating Profit (£m)

Year to March 2012	£101.7m
Year to March 2011	£103.7m
Decrease (%)	1.9%

b) Capital Expenditure (£m)

Year to March 2012	£82.8m
Year to March 2011	£61.7m
Increase (%)	34.2%

c) Electricity Distributed (TWh)

Year to March 2012	8.1 TWh
Year to March 2011	8.5 TWh
Decrease (%)	4.7%

d) Customer Minutes Lost

Year to March 2012	73
Year to March 2011	78
Decrease (%)	6.4%

Operating and Financial Review (continued)

Business performance overview (continued)

e) Customer Interruptions – number per 100 customers

Year to March 2012	71
Year to March 2011	74
Decrease	4.1%

The decrease in operating profit principally reflects an under recovery of allowed regulatory income in 2011/12, along with an over recovery in 2010/11, and a reduction in connection activity. Regulated revenue is recovered by the Company by means of tariffs provided to electricity suppliers, and therefore collected on the basis of volume of electricity used by end customers. A reduction in demand will result in an under recovery in revenue in any given year. However, as the allowed revenue for each year is agreed with Ofgem, any difference is purely timing, and any under recovery will be recovered in future years. Therefore the decrease in revenue in 2011/12 from the allowed position will see an equivalent over recovery in future years to compensate. In addition there was an increase in fault-related costs on the network as a result of a significant increase in the year of severe weather-related events.

The total volume of electricity distributed by the Company during 2011/12 was 8.1TWh, compared with 8.5TWh in the previous year. This reflects the milder weather conditions experienced in 2011/12.

Incentive income and other additional allowances

Performance in respect of both customer minutes lost and customer interruptions was improved from the prior year and ahead of the targets set by Ofgem under its Interruptions Incentive Scheme (IIS), which gives financial benefits to distribution network operators that deliver good performance for customers. Performance-based income covers a number of issues, including the quality of service provided to customers and innovation.

As a result of operational performance during 2011/12 the Company expects to earn additional incentive income and allowances (excluding losses) of £4.1m (2010/11: £2.6m). This reflects effective investment in the automation of the networks, effective operational responses to electricity supply interruptions and continued investment in innovation.

Responding to effects of severe weather

In the winter of 2011/12, the Company's electricity networks were subjected to the effects of severe weather on an unusually large number of occasions, including the 3rd of January storm affecting the north of Scotland. This weather event alone, featuring exceptional low altitude wind speeds of over 90 miles per hour, resulted in 600 separate faults and over 1,000 points of damage on the network and the loss of power to around 40,000 households. The equivalent of three months of fault repair work was carried out in four days (with very high winds also occurring on 4 January) and was marked by the commitment of employees and the patience on the part of affected communities. The efforts of the Company and other service providers were praised by the Scottish Government. This storm event and a number of other weather events were treated as exceptional by Ofgem, meaning that they are excluded from the calculation of performance measures such as customer minutes lost.

Operating electricity networks efficiently

Efficiency is one of the Group's and Company's core values and amongst Ofgem's explicit purposes in setting Price Controls is to keep as low as possible the costs of providing secure and reliable networks. The Company has a straightforward operating model, under which the vast majority of activities are in-house. Under this model:

- customer-facing activities, such as restoring power supplies or providing new connections, are managed from a network of 7 depots in communities throughout the north of Scotland; and
- network management activities, such as inspections, maintenance and investment, are carried out in Operational Production Groups.

This model gives the Company a strong oversight of operations and investment, allows flexibility in responding to changed circumstances and supports a culture of efficiency, teamwork and excellence, including innovation.

Operating and Financial Review (continued)

Electricity network investment

2011/12 was the second year of the electricity Distribution Price Control for 2010-15. The Price Control changed the framework for operating and capital expenditure to remove the perceived bias in favour of the latter and to ensure the delivery of not only the investment itself but of agreed outputs from it. The most successful electricity distribution companies, therefore, will be those that apply efficiency and innovation to maximise outputs from agreed expenditure.

In response to this, the company has identified a number of solutions and interventions for wider deployment in 2010-15 to ensure its success throughout the Price Control period. This means the Company has robust and cost efficient network investment processes that deliver real value for customers. It has also identified a number of important innovations and new technologies that are delivering cost savings and minimising disruption.

For example, in rural areas, use of the Ordnance Survey's Imagery database of aerial photography has provided a simple and effective way of surveying thousands of kilometres of overhead lines for potential risk of tree damage. In urban areas, the Company has used directional drill technology, which creates minimum disturbance to the highway and thereby reduces disruption to the public and the cost of reinstatement, to install new circuits.

The deployment of innovations and technologies such as these, plus good performance in response to Ofgem's enhanced incentive mechanisms in areas such as customer service should enable the Company to continue to achieve the post-tax real return in excess of 5% which it is targeting in electricity distribution.

Against this background, capital expenditure in electricity distribution networks by the Company was £82.8m in 2011/12. As at 31 March 2012, the Company's estimate of Ofgem's valuation of the assets of its electricity distribution business (the Regulated Asset Value, or RAV) was £940m based on Ofgem's methodology. The need for further significant investment in Great Britain's electricity distribution networks, to maintain and/or replace ageing assets or to provide additional capacity, is likely to mean the Company will invest around £80m in 2012/13, taking the total for the first three years of the 2010-15 Price Control to around £225m. As a result, the RAV of the Company's electricity distribution network should increase to around £970m over the course of the year.

Significant developments include plans to invest in the resilience of the electricity network in Argyll and Bute, which was particularly affected by the storms of 2011/12, including provision of underground cables in Dunoon and of large-scale mobile generation connection points for Bute.

Making electricity networks smart

Although there is no standard definition, the European Technology Platform for the Electricity Networks of the Future defines smart grids as 'electricity networks that can intelligently integrate the behaviour and actions of all users connected to it - generators, consumers and those that do both - in order to efficiently deliver sustainable, economic and secure electricity supplies'.

The next decade promises major technological change for electricity distribution networks as a result of things like micro generation, the growth of electricity as a source of heating and electric vehicles. All of this will change the traditional flows of electricity, which means smarter, more dynamic networks will be required.

The Group, together with the Company and Smarter Grid Solutions Ltd, an associate company, 'switched on' the UK's first commercial smart grid technology on its power distribution network on Orkney in 2009. This has since allowed 20MW of additional capacity for generating electricity to be connected to the network, at a small fraction of the cost that would have been required had traditional means been adopted.

Operating and Financial Review (continued)

Making electricity networks smart (continued)

Another major 'smart' project, with total spend of £5.1m to 31 March 2012, is being led by the Company;

- **Northern Isles New Energy Solutions (NINES) in Shetland:** NINES is a pilot project representing the first stage of the Integrated Plan for managing electricity supply and demand on Shetland, which the Company is required by Ofgem to present in 2013. It features the use of heat and electricity storage to manage intelligently the impact of movements in demand on electricity generation in Shetland, which could allow more renewable energy to be connected to the network. It also features new active network management solutions. In September 2011, Ofgem announced that the NINES should be funded as part of the Integrated Plan, with 85% of its expenditure included in the Company's RAV and the remaining 15% included in the Company's allowed revenue. This confirmed that NINES is not just a 'smart' programme but a comprehensive and sustainable solution to the energy challenges on Shetland which is designed to meet the needs and aspirations of the community.

Supporting deployment of electric vehicles

Electric vehicles (EVs) will be an essential part of the move towards a low-carbon transport infrastructure. Current predictions suggest that EVs could account for as many as 10% of new car sales by 2020. The challenge for electricity distribution companies is to prepare their networks for the likely upswing in demand arising from EVs, and SSE plc together with the Company was a full participant in two EV projects, both supported by the Technology Strategy Board - the MINI E and the Ford Transit Connect consortia.

These have helped to demonstrate that up to one in four homes will be able to have an EV without it having a significant impact on the electricity network. Nevertheless, other issues – such as the need to schedule re-charging effectively and to develop new control systems – require significant attention and the Company is carrying out further work to understand the requirements of so-called "smart charging" to maximise use of the existing infrastructure.

Regulatory environment

2011/12 was the second year of a five-year price control period known as Distribution Price Control Review 5. Ofgem has now commenced planning for the next price control period for electricity distribution, under the RIIO ("Revenue = Incentives+Innovations+Outputs") framework. Amongst other things, this framework is designed to place additional onus on licensees to perform against agreed sets of targets, with the ability to gain extra income (or indeed to sacrifice income) depending on performance. The first RIIO distribution price control for electricity distribution, known as RIIO ED1, will start in 2015/16 and will run for at least 8 years.

Understanding and adapting to any new regulatory environment is critical to the successful operation of the Company. As a result, the Company is putting in place plans now to address this new environment, and will publish its business plan setting out its vision for how it will address the challenges of RIIO ED1 in early 2013. Senior management are actively engaging with Ofgem on its future plans to ensure the best possible outcome for the Company.

Factors affecting the development of the business

During 2012/13 and beyond the Company's priorities in Electricity Distribution are to:

- comply fully with all safety standards and environmental requirements;
- ensure that the networks are managed as efficiently as possible, delivering required outputs while maintaining tight controls over operational expenditure;
- put responsiveness at the heart of day-to-day operations, so that the number and duration of power cuts experienced by customers is kept to a minimum;
- ensure there is adequate capacity to meet changing demands on the electricity system;
- deliver excellent service to customers, which responds effectively to their needs during supply interruptions and in 'business-as-usual' situations; and
- make progress on the deployment of innovative investment in smart grids.

With such significant changes required over the next few years, not least in adapting the networks to accommodate changes in production and consumption, the scope for additional incremental growth in electricity distribution networks is clear.

Operating and Financial Review (continued)

Factors affecting the development of the business (continued)

In addition to the changing nature of the electricity networks and the regulatory environment, other factors which would affect the longer term performance of the business would include the macroeconomic situation and impact on the Company's funding costs, and the performance of the Company and its contractors on large capital projects. The former is addressed by SSE plc's group treasury policies to ensure that appropriate funding is available to the business. The latter is addressed by use of the Group's Large Capital Project Governance Framework which is designed to ensure projects are governed, developed, approved and executed in an effective manner. All significant distribution projects are governed by this framework.

Safety

The Company believes that all work can be done in such a way that no-one, whether an employee, contractor, customer or member of the community, suffers from its operations. It believes that all injuries are preventable and it aims to provide staff with training, work methods and equipment to achieve that goal. Safety is the first of the Group's core values. In line with this, the Group's Safety, Health and Environment Manual, which has the status of a work instruction, emphasises that safety will not be compromised for business interest or operational pressures and all injuries, plant damage and near misses will be reported and investigated. The Group Safety, Health and Environmental Advisory Committee, together with the Group Audit Committee and management, ensures that: health, safety and environmental policy statements are being adhered to; sets health, safety and environmental targets for the Group; and monitors the performance of the Group against these targets.

As a result of this commitment to safety, both the Group and the Company continue to be at the forefront of Britain's electricity industry in relation to safety.

Employees

The Group believes that there is a commonality of interest between employees, customers and shareholders. To reinforce this it provides opportunities for employees to become and remain shareholders in the Group through a Share Incentive Plan and a Sharesave Scheme. Employee participation in these schemes is now 43% and 35% respectively across the Group.

Within the Group, employee participation is encouraged through adherence to the Company's Teamwork value, which states: 'We support and value our colleagues and enjoy working together in an open and honest way.' The appraisal process for employees, including the senior management team, specifically evaluates their performance in Teamwork, along with performance in respect of the Group's other core values: Safety, Service, Efficiency, Sustainability and Excellence. In keeping with these values, the Group produced and distributed to all employees in March 2010 a comprehensive code of business practice, 'Doing the right thing'. It highlights, summarises and complements a range of ethics-related policies which the Group has in place.

In addition to a wide range of internal communication media and events, employee participation in the Group is also encouraged through the Chief Executive's blog, inter-active online forums, division and subject-specific employee surveys, Director-led regional roadshows and the Licence to Innovate scheme, which enables employees to research, review and test-trial new ideas.

Resources Available

As part of the SSE plc group, the Company has significant resources which it can draw upon to meet its service commitments. The Company benefits from group-wide treasury management functions in order to provide adequate financing, with undrawn facilities totalling £1bn available to SSE plc which could be made available to the Company as required. The Company also draws upon shared services covering central functions such as finance, HR, regulation, health and safety, company secretarial and insurance services. All such services are provided under an appropriate Service Level Agreement.

The Company has 735 employees which it calls on to maintain its distribution network and carry out investment in future developments. In addition to these employees, the services of key contractors are called upon in a number of large capital projects to ensure that these projects are delivered on time and on budget. Where possible and economically efficient for the Company, these contractors are provided by other SSE group companies, reducing reliance on external companies.

Operating and Financial Review (continued)

Social and Community Issues

The Company considers its relationship with the community it serves as a core part of its operations. Engagement with local users and the wider stakeholder community is a fundamental principle underlying the RIIO ED1 price control, and the Company has a detailed stakeholder engagement plan in place to ensure that it is sufficiently informed by its customers and the community which it serves. The Business Plan which the Company will submit to Ofgem as part of that price control will detail the areas on which stakeholders will be consulted, their responses, and how those responses will be used to shape our Business Plan and associated capital expenditure projects.

On a wider basis, the Company participates in SSE plc's programme of community-based schemes, which focus on employee volunteering, visitor facilities in Dorset, Cheshire and Perth, financial support for community programmes, and support for the work of schools through the Eco Schools project. SSE plc made payments totalling £6.1m to charitable and community programmes in the UK and Ireland in 2011/12.

Key Contractual Arrangements

The Directors consider the Service Level Agreement in place between the Company and SSE Services plc for the provision of corporate services to be essential for the continuance of the Company's operations in the short-to-medium term.

There are a number of contracts with both internal and external parties for the provision of services to maintain and develop the Company's distribution network. It is not believed that any of these contracts are of sufficient size or concentration to result in a dependence on any one external supplier.

Capital Structure

The Company regards its capital as comprising its equity, cash and borrowings. Its objective in managing capital is to maintain a strong balance sheet and credit rating so as to maintain investor, creditor and market confidence and to sustain future development of the business. The capital structure is kept under review and the Group and Company both continue to maintain one of the strongest balance sheets in the global utility sector. This gives the Company significant competitive advantage in terms of cost of funding and supporting new developments.

Treasury Policy, Objectives and Financial Risk Management

The Company's operations are generally financed by a combination of retained profits, bank borrowings, long term debt issuance and inter company loan balances. As a matter of policy, a minimum of 50% of the Company's debt is subject to fixed or inflation linked rates of interest. Within this policy framework, the Company borrows, as required, on different interest bases, with derivatives and forward rate agreements being used to achieve the desired out-turn interest rate profile. Borrowings of the Company are mainly made in Sterling to reflect the underlying currency denomination of assets and cashflows within the Company. Further details of the Company's borrowings can be found in note 14 of the notes to the financial statements.

The Company's financial risk is managed as part of the wider Group risk management policy. For more information regarding this please visit the Group's 2012 Annual Report at www.SSE.com.

The main financial risks affecting the Group, and therefore the Company, include exposures to fluctuations or changes in interest rates, foreign exchange rates, liquidity, commodity prices and volumes and counterparty creditworthiness.

The Group's Risk and Trading Committee, which reports to the Group Board, reviews and agrees policies for addressing each of these risks. At 31 March 2012, 77.4% of the Group's borrowings were at fixed or inflation-linked interest rates, after taking account of interest rate swaps. The Company's main risk area is in relation to interest rates and, as noted, this is controlled as part of the Group's risk management policies.

Operating and Financial Review (continued)

Liquidity

The Company's exposure to liquidity risk is managed centrally by the Group's Treasury function. Short term liquidity is reviewed daily by Treasury, while the longer term liquidity position is reviewed on a regular basis by the Management Board. In relation to the Group's liquidity risk, the Group's and therefore Company's policy is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation. It does this by ensuring that the Group has available committed borrowings and facilities equal to at least 105% of forecast borrowings over a rolling 12 month period.

Taxation

The Company's effective current tax rate was 24.3% compared with 25.8% in the previous year after prior year adjustments. The headline effective tax rate, which includes the impact of substantively enacted changes in the UK corporation tax rate, is 9.5% compared with 15.9% in the previous year.

Dividend

Following a review of distributable reserves, the Directors declared, approved and paid a dividend of £100.0m (2011 – £10.0m) in the year.

Borrowings and Facilities

The Company has loans of £493.4m (2011 – £487.7m) of which £300.0m (2011 – £300.0m) is due to other Group companies and £193.4m (2011 – £187.7m) is in the form of loans from the European Investment Bank and an index-linked bond. Of the total, interest is paid at fixed or inflation-linked rates on £468.4m (2011 – £462.7m).

As at 31 March 2012, the weighted average interest rate payable was 4.71% (2011 – 4.75%) and the weighted average remaining term was 16.93 years (2011 – 17.32 years).

Pensions

58% of employees of the Company are members of the Scottish Hydro-Electric Pension Scheme, which, at 31 March 2012 on an IAS 19 basis adjusted for IFRIC 14 had a deficit, net of deferred tax, of £149.1m included in the Group accounts (2011 – £177.5m).

International Financial Reporting Standards

The application of International Financial Reporting Standards (IFRS) is required for listed companies for accounting periods commencing on or after 1 January 2005. As a result, the Group's financial statements for the year to 31 March 2012 have been prepared in accordance with EU adopted IFRS. The financial statements of Scottish Hydro Electric Power Distribution plc have been prepared in accordance with applicable UK Generally Accepted Accounting Principles (UK GAAP).

Corporate Governance Statement

As a subsidiary company of SSE plc, ("The Group"), Scottish Hydro Electric Power Distribution plc ("The Company") operates within the Group's corporate governance framework. The Company does not have listed shares and therefore is not subject to the Combined Code on Corporate Governance.

The Group's corporate governance policies are described in the SSE plc's annual report and accounts 2012 under corporate governance on pages 61 to 64.

The Board of SSE plc considers that it complied in full with the combined code during 2011/12.

SSE plc Group ("The Group")

The Board is collectively responsible to the Group's shareholders for the long-term success of the Group and for its overall strategic direction, its values and its governance. It provides the leadership necessary for the Group to meet its business objectives whilst ensuring that a sound system of internal control and risk management is in place.

The Group's core purpose is to provide the energy people need in a reliable and sustainable way while abiding by its core values: safety; service; efficiency; sustainability; excellence; and teamwork.

The Board continues to be committed to ensuring that the highest standards of corporate governance are maintained. The Board confirms that it has, throughout the period under review, complied with all provisions set out in the Code, except in respect of Code Provision D.2.1 for a short period. More details of this can be found in SSE plc's annual report on page 61.

The Board comprises the Chairman, three Executive Directors and six independent non-Executive Directors. This gives the Board a good balance of independence and experience, ensuring that no one individual or group of individuals has undue influence over the Board's decision making.

There are four principal Board committees; an Audit Committee, a Remuneration Committee, a Health, Safety and Environmental Advisory Committee and a Nomination Committee and details of the appointees and work undertaken by these committees are included in the published Annual Report of the Group, a copy of which is on the Group website (www.sse.com).

Following a competitive tender, KPMG Audit Plc has been the external auditor of the enlarged Group since 1999. Under its terms of reference, the Audit committee has responsibility for recommending to the Board removal of the external Auditors. The Audit Committee considers that the relationship with the Auditors is working well and remains satisfied with their effectiveness. Accordingly, it has not considered it necessary to require the firm to tender for the audit work. There are no contractual obligations restricting the Company's choice of external auditor. The external Auditors are required to rotate the audit partner's responsible for the Group audit every five years and the current lead partner has been in place for three years.

Scottish Hydro Electric Power Distribution Limited ("The Company")

Board of Directors

The Board consists of six Directors, one of whom is a Director of the Group. None of the Directors are Directors of Group Companies involved in Retail or Wholesale activities. Company Board meetings and sub committee meetings were held on 9 occasions during the course of the year. There are no non-executive or independent directors. The Board does not have a separately appointed chairman. Meetings are chaired by a member of the Board. The Board of the Company does not have a Nominations, Remuneration or Audit Committee. These functions are dealt for the Company in conjunction with the relevant committee of the SSE plc ('the Group') Board.

Attendance at meetings of the Board during 2011/12, expressed as a number of meetings attended out of number eligible to attend is set out below:

Corporate Governance Statement (continued)

Scottish Hydro Electric Power Distribution plc ("The Company")

Board of Directors

Director	Attendance
Gregor Alexander	9 of 9
Steven Kennedy	9 of 9
Mark Mathieson	8 of 9
Ian Funnell	6 of 8
Aileen McLeod	9 of 9
Stuart Hogarth	6 of 7
Colin Hood (resigned 15 September 2011)	1 of 3

Internal Control

The Directors acknowledge that they have responsibility for the Company's systems of internal control and risk management and for monitoring their effectiveness. The purpose of these systems are to manage, rather than eliminate, the risk of failure to achieve business objectives, and provide reasonable assurance as to the quality of management information and to maintain proper control over the income, expenditure, assets and liabilities of the Company.

No system of control can, however, provide absolute assurance against material misstatement or loss. Accordingly, the Directors have regard to what controls, in their judgement, are appropriate to the Company's business, to the materiality of the risks inherent in the business, and to the relative costs and benefits of implementing specific controls. This process is regularly reviewed by the Board and has been in place for the whole year.

Control is maintained through: an organisation structure with clearly defined responsibilities, authority levels and lines of reporting; the appointment of suitably qualified staff in specialised business areas; and continuing investment in high quality information systems. These methods of control are subject to periodic review as to their implementation and continued suitability.

There are established procedures in place for regular budgeting and reporting of financial information. The Company's performance is reviewed by the Board as well as the Group Board. Reports include variance analysis and projected forecasts of the year compared to approved budgets and non-financial performance indicators.

There are Group policies in place covering a wide range of issues and risks such as financial authorisations, IT procedures, health, safety and environmental risks, crisis management, and a policy on ethical principles. The business risks associated with the Company's operations are regularly assessed by the Directors.

The effectiveness of the systems of internal control is monitored by the Group internal audit department. Their reports, which include where appropriate relevant action plans, are distributed to senior managers and Directors.

Environment

The Group manages a wide range of environmental issues. Operating the power systems network is recognised as a priority area and formal environmental management systems have been developed. The systems have five main elements, based on the established management cycle of (1) setting policy, (2) planning, (3) implementing and operating, (4) checking and correcting and (5) reviewing.

The system exists to enable managers to deliver the Group's environmental policies through procedures and work instructions. It reflects an integrated, Group-wide health and safety and environmental management system.

Going Concern

The Directors consider that the Company has adequate resources to continue in operational existence for the foreseeable future. The financial statements are therefore prepared on a going concern basis.

Report of the Directors

The Directors present their report together with the audited Financial Statements for the year ended 31 March 2012.

1. Principal Activities

The Company's principal activity during the year was the regulated distribution of electricity.

2. Business Review

The Company is responsible for managing an electricity distribution network, serving around 746,000 customers in the North of Scotland. Distribution of electricity and the level of capital investment within the network area is a monopoly activity and is closely regulated by the Office of Gas and Electricity Markets (Ofgem) within a framework known as the Price Control. The Company also carries out the business of provision of new electrical connections services within its licensed area and the construction and management of out-of-area electricity networks in Scotland. A full review of the year is contained within the Operating and Financial Review section of these Accounts.

3. Results and Dividends

The profit for the financial year amounted to £58.1m (2011 - £63.5m). A final dividend of £100.0m (2011 - £10.0m) was declared, approved and paid by the Board during the year.

4. Directors

The Directors who served during the year were as follows:

Gregor Alexander
Steven Kennedy
Mark Mathieson
Ian Funnell
Aileen McLeod
Stuart Hogarth
Colin Hood (resigned 15 September 2011)

5. Political and Charitable Donations

During the year, no charitable or political donations were made.

6. Employment Policies

Staff are actively encouraged to be involved in Company affairs in a wide variety of ways. These include monthly team meetings, briefing documents and internal videos. Policies on such matters as Equal Opportunities and Health and Safety are regularly communicated to staff and involvement is supported through local committees. New staff joining the Company receive induction training.

It is Company policy, where possible, to provide employment opportunities for disabled people. Staff who become disabled are supported in continuing employment through identification of suitable jobs and the provision of necessary retraining.

7. Supplier Payment Policy

It is the Group and Company's policy that payment terms are agreed at the outset of a transaction and are adhered to; that bills are paid in accordance with the contract; and that there are no alterations to payment terms without prior agreement. The number of suppliers days represented by trade creditors was 37 days at 31 March 2012.

Report of the Directors (continued)

8. Auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware; and each director has taken all the steps that ought to have been taken as a director to be aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

In accordance with Section 489 of the Companies Act 2006, a resolution for the re-appointment of KPMG Audit Plc as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.

ON BEHALF OF THE BOARD

L. Manderson

Lilian Manderson
Company Secretary
20 July 2012

Statement of directors' responsibilities in respect of the Directors' Report and the Financial statements

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

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

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc

We have audited the financial statements of Scottish Hydro Electric Power Distribution plc for the year ended 31 March 2012 as set out on pages 14 to 34. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 12, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's web-site at www.frc.org.uk/apb/scope/private.cfm.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2012 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

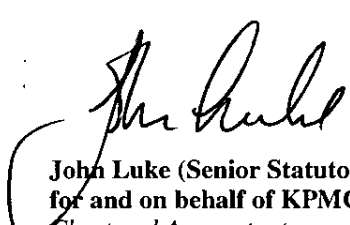
Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



John Luke (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants

Saltire Court
20 Castle Terrace
Edinburgh
EH1 2EG

31 July 2012

Scottish Hydro Electric Power Distribution plc
31 March 2012

Profit and Loss Account
for the year ended 31 March 2012

	Note	2012 £m	2011 £m
Turnover		302.2	301.9
Cost of sales		(63.1)	(70.1)
Gross profit		239.1	231.8
Distribution costs		(122.7)	(116.1)
Administrative costs		(14.7)	(12.0)
Operating profit	2	101.7	103.7
Net interest payable	5	(37.5)	(28.2)
Profit on ordinary activities before taxation		64.2	75.5
Tax on profit on ordinary activities	6	(6.1)	(12.0)
Profit for the financial year	17	58.1	63.5

The above results are derived from continuing activities.

The accompanying notes are an integral part of these Financial statements.

Scottish Hydro Electric Power Distribution plc
31 March 2012

Statement of Total Recognised Gains and Losses
for the year ended 31 March 2012

	2012 £m	2011 £m
Profit for the financial year	58.1	63.5
Gain on effective portion of cash flow hedges (net of tax)	0.1	1.1
Total recognised gains and losses relating to the financial year	58.2	64.6

Reconciliation of Movements in Shareholders' Funds
as at 31 March 2012

	Note	2012 £m	2011 £m
Profit for the financial year		58.1	63.5
Dividends	7	(100.0)	(10.0)
Credit in respect of employee share schemes (net of tax)		0.9	0.9
Gain/(loss) on effective portion of cash flow hedges (net of tax)		0.1	1.1
Net (reduction)/ addition to shareholders' funds		(40.9)	55.5
Opening shareholders' funds		460.2	404.7
Closing shareholders' funds		419.3	460.2

Scottish Hydro Electric Power Distribution plc
31 March 2012

Balance Sheet
as at 31 March 2012

	Note	2012 £m	2011 £m
Fixed Assets			
Tangible assets	9	896.8	854.9
Current assets			
Stocks	10	1.8	1.7
Debtors:			
Amounts falling due within one year	11	456.6	420.7
Amounts falling due after more than one year	11	22.4	22.4
Total debtors		479.0	443.1
Total current assets		480.8	444.8
Creditors			
Amounts falling due within one year	12	(277.5)	(144.1)
Net current assets		203.3	300.7
Total assets less current liabilities		1,100.1	1,155.6
Creditors:			
Amounts falling due after more than one year	13	(556.8)	(575.4)
Derivative financial liabilities	20	(23.7)	(10.8)
Provisions for liabilities and charges			
Deferred taxation	15	(100.3)	(109.2)
Net assets		419.3	460.2
Capital and reserves			
Called up share capital	16	62.0	62.0
Profit and loss account	17	358.8	399.8
Hedge reserve	17	(1.5)	(1.6)
Shareholders' funds		419.3	460.2

These Financial Statements were approved by the Directors on 20 July 2012 and signed on their behalf by



Gregor Alexander, Director

Scottish Hydro Electric Power Distribution plc, Registered No. 213460

Scottish Hydro Electric Power Distribution plc
31 March 2012

Cash Flow Statement
for the year ended 31 March 2012

	Note	2012 £m	2011 £m
Net cash inflow from operating activities	22	219.3	101.4
Interest received		7.4	1.9
Interest paid		(26.4)	(25.8)
Returns on investments and servicing of finance		(19.0)	(23.9)
Corporation tax paid		(19.8)	(28.7)
Taxation		(19.8)	(28.7)
Cash received on assumption of business from related party	8	-	23.0
Purchase of tangible fixed assets		(80.5)	(61.8)
Capital expenditure and financial investment		(80.5)	(38.8)
Equity dividends paid	7	(100.0)	(10.0)
Net cash inflow before management of liquid resources and financing		-	-
Repayment of borrowings		-	-
New borrowings		-	-
Financing		-	-
Increase/(decrease) in cash in the year		-	-

**Notes on the Financial statements
for the year ended 31 March 2012**

1. Significant accounting policies

Basis of preparation

The Financial Statements have been prepared under the historical cost convention and in accordance with UK generally accepted accounting standards (UK GAAP). The principal accounting policies are summarised in the Notes to the Financial statements and have been applied consistently.

As the Company is a wholly owned subsidiary of SSE plc (the "Group"), it has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the SSE (the "Group").

It has also taken advantage of the exemption contained in FRS 29 and has therefore not prepared the disclosures relating to financial instruments and capital as full disclosure is provided in Group financial statements.

Turnover

Turnover comprises the value of electricity distribution services and facilities provided during the year. Turnover includes an estimate of the value of the distribution of electricity on behalf of customers between the date of the last meter reading and the year-end. In addition, turnover is also recognised on the value of customer contributions towards new connections, diversions and modifications to existing networks that occurred in the year.

Research and development

Expenditure on research and development is charged to the profit and loss account as incurred.

Taxation

The charge for taxation is based on the profit for the year and takes into account deferred taxation.

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

Deferred taxation arises in respect of all items where there are timing differences between their treatment for accounting and taxation purposes. This is recognised where an obligation to pay more tax in the future has originated but not reversed at the balance sheet date. A deferred tax asset is recognised only when it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Tangible fixed assets

(i) Depreciation

Heritable and freehold land is not depreciated.

Depreciation is provided on tangible fixed assets to write off cost, less residual values, on a straight-line basis over their estimated operational lives. The estimated operational lives are as follows:

	Years
Distribution assets	10 to 80
Non-operational assets	
Buildings - freehold	Up to 60
- leasehold	Lower of lease period and 60
Fixtures, equipment, plant and machinery, vehicles and mobile plant	4 to 10

(ii) Subsequent expenditure

Expenditure incurred to replace a component of a tangible fixed asset that is accounted for separately is capitalised. Other subsequent expenditure is capitalised only when it increases the future economic benefits of the tangible fixed asset to which it relates.

**Notes on the Financial statements
for the year ended 31 March 2012**

1. Significant accounting policies (continued)

Customer contributions

Customer contributions towards construction or acquisition of new Out-of-Area networks and capital grants are recorded as deferred income and released to the profit and loss account over the estimated life used in calculating contributions. Deferred income also includes outstanding balances of customer contributions on new connections to existing networks pre business separation in 2001.

Stocks and work in progress

Stocks are valued at the lower of cost and net realisable value. The valuation of work in progress is based on the cost of labour, plus appropriate overheads and the cost of materials. Progress invoices are deducted in arriving at the amounts stated.

Employee benefit obligations

Pensions

The Group operates a number of pension schemes on behalf of employees. The amounts charged represent the contributions payable to the schemes in the year and are charged directly to the profit and loss account as incurred.

Equity and equity-related compensation benefits

SSE plc, the ultimate parent of the Company, operates a number of All Employee Share Schemes as described in the Remuneration Report of the Group. These schemes enable Group employees to acquire shares of the ultimate parent company. The employees of the Company are entitled, where applicable, to participate in these schemes. The Company has not been charged with the cash cost of acquiring shares on behalf of its employees, this cost is borne by the Ultimate Parent Company. Where the fair value of the options granted has been measured, the Company has recognised the expense as if the share based payments related to the Company's own shares.

The exercise prices of the sharesave scheme are set at a discount to market price at the date of the grant. The fair value of the sharesave scheme option granted is measured at the grant date by use of a Black-Scholes model. The fair value of the options granted is recognised as an expense on a straight-line basis over the period that the scheme vests. Estimates are updated at each balance sheet date with any adjustment in respect of the current and prior years being recognised in the profit and loss accounts.

The costs associated with the other main employee schemes, the share incentive plan and the deferred bonus scheme, are recognised over the period to which they relate.

Dividends on shares presented within shareholders' funds

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. Unpaid dividends that do not meet these criteria are disclosed in the notes to these accounts.

Financial instruments:

The Company adopted FRS 25 and FRS 26 with effect from 1 April 2005. FRS 26 requires that financial instruments are initially recognised and subsequently measured at fair value. Financial assets and liabilities are recognised when the Company becomes a party to the provisions of the instrument.

Recognition of profits on contracts

Profit is recognised on long-term contracts on completion of the total contract. Provision is made for foreseeable losses.

**Notes on the Financial statements
for the year ended 31 March 2012**

1. Significant accounting policies (continued)

Accounting policies under FRS 25 and 26

i) Interest Rate Derivatives

Financial derivative instruments are used by the Company to hedge interest rate exposures. All such derivatives are recognised at fair value and are re-measured to fair value in each reporting period. Certain derivative financial instruments are designated as being held for hedging purposes. The designation of the hedge relationship is established at the inception of the contract and procedures are applied to ensure the derivative is highly effective in achieving its objective and that the effectiveness of the hedge can be reliably measured. The treatment of gains and losses on re-measurement is dependent on the classification of the hedge and whether the hedge relationship is designated as either a 'fair value' or 'cash flow' hedge. Derivatives that are not designated as hedges are treated as if held for trading, with all fair value movements attributable to the risk being hedged recorded through the profit and loss account.

A derivative classified as a 'fair value' hedge recognises gains and losses from re-measurement immediately in the profit and loss account. Loans and borrowings are measured at cost except where they form the underlying transaction in an effective fair value hedge relationship. In such cases, the carrying value of the loan or borrowing is adjusted to reflect fair value movements with the gain or loss being reported in the profit and loss account.

A derivative classified as a 'cash flow' hedge recognises the portion of gains or losses on the derivative which are deemed to be effective directly in equity in the hedge reserve. Any ineffective portion of the gains or losses is recognised in the profit and loss account. The gains or losses that are recognised directly in equity are transferred to the profit and loss account in the same period in which the forecast transaction actually occurs.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecast transaction occurs. If the transaction is no longer expected to occur, the cumulative gain or loss recognised in equity is recognised in the profit and loss account.

ii) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Company's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

iii) Debtors

Debtors do not carry any interest and are measured at cost (less an appropriate allowance for irrecoverable balances).

iv) Interest-bearing loans and borrowings

All such loans and borrowings are initially recognised at fair value including transaction costs and are subsequently measured at amortised cost, except where the loan or borrowing is the hedged item in an effective fair value hedge relationship.

v) Share Capital

Ordinary shares are accounted for as equity. Costs associated with the issue of new shares are deducted from the proceeds of issue.

**Notes on the Financial statements
for the year ended 31 March 2012**

2. Operating profit

Operating profit is arrived at after charging / (crediting):

	2012 £m	2011 £m
Depreciation of tangible fixed assets	40.9	39.6
Operating lease rentals	0.6	0.5
Release of deferred income in relation to customer contributions and capital grants	(3.4)	(3.4)
Research and development	1.4	2.4
Net management fee in respect of services provided by group companies	15.1	12.0

The Company incurred an audit fee of £0.06m (2011 - £0.06m) in the year.

3. Staff costs and numbers

	2012 £m	2011 £m
Staff costs:		
Wages and salaries	26.1	25.4
Social security costs	2.7	2.3
Share based remuneration	0.9	1.0
Other pension costs (note 18)	23.0	22.5
	52.7	51.2

Less capitalised as tangible fixed assets	(19.2)	(18.3)
	33.5	32.9

Employee numbers

	2012 Number	2011 Number
Numbers employed at 31 March	735	711

	2012 Number	2011 Number
The monthly average number of people employed by the Company during the year	724	706

4. Directors' remuneration

The level of emoluments of the Directors employed by the Company were as follows:

	2012 £m	2011 £m
Remuneration as executives	0.4	0.4

**Notes on the Financial statements
for the year ended 31 March 2012**

5. Net interest payable

	2012 £m	2011 £m
Interest receivable:		
Interest due from group companies	7.4	1.9
	<u>7.4</u>	<u>1.9</u>
Interest payable:		
Bank loans and overdrafts	(12.6)	(13.7)
Interest due to group companies	(18.5)	(17.9)
	<u>(31.1)</u>	<u>(31.6)</u>
Movement on financing derivatives	(13.8)	1.5
Net interest payable	<u>(37.5)</u>	<u>(28.2)</u>

6. Taxation

	2012 £m	2011 £m
Current tax:		
UK corporation tax on profits of the year	18.8	24.2
Adjustments in respect of prior years	(3.2)	(4.7)
	<u>15.6</u>	<u>19.5</u>
Deferred tax:		
Origination and reversal of timing differences	(1.9)	(2.9)
Effect of tax rate change	(8.4)	(8.4)
Adjustment in respect of previous year	0.8	3.8
Total Deferred Tax	<u>(9.5)</u>	<u>(7.5)</u>
Total tax on profit on ordinary activities	<u>6.1</u>	<u>12.0</u>

The difference between the total current tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax is as follows:

	2012 £m	2011 £m
Profit before tax	64.2	75.5
Tax on profit on ordinary activities at standard UK corporation tax rate of 26% (2011 - 28%)	16.7	21.1
Effects of:		
Depreciation in excess of capital allowances	2.9	4.0
Depreciation of non qualifying assets	0.2	0.1
Share based remuneration	0.1	0.1
Other timing differences	(1.1)	(1.1)
Adjustments in respect of prior years	(3.2)	(4.7)
Current tax charge for year	<u>15.6</u>	<u>19.5</u>

(i) The 2012 Budget on 21 March 2012 announced that the UK corporation tax will reduce to 22% by 2014. A reduction in the rate from 26% to 25% (effective from 1 April 2012) was substantively enacted on 3 July 2011, and further reductions to 24% (effective from 1 April 2012) and 23% (effective from 1 April 2013) were substantively enacted on 26 March 2012 and 3 July 2012 respectively. This will reduce the Company's future tax charge accordingly, and further reduce the deferred tax liability at 31 March 2012 (which has been calculated based on the 24% substantively enacted at the balance sheet date) by £8.4m. It has not yet been possible to quantify the full anticipated effect of the announced further 1% rate reduction, although this will further reduce the Company's future tax charge and reduce the Company's deferred tax liability accordingly.

**Notes on the Financial statements
for the year ended 31 March 2012**

7. Dividends

	2012	2011
	£m	£m
Amounts recognised as distributions from equity:		
Final dividend of 161.3p (2011 – 16.1p) per share	100.0	10.0

The final dividend for the current year, £100.0m (2011 – £10.0m), was declared and approved on 23 March 2012 and was paid to shareholders on 31 March 2012.

8. Acquired business

There were no acquisitions in the current year.

During the prior year, the Company acquired the electrical connections business, relating to distribution network connections in the Company's licensed area and the portfolio of out of area electricity networks in the rest of Scotland, both of which were previously owned and managed by S+S Limited, a related company. The transaction was part of a re-organisation within the SSE plc Group and was made to conform with the regulatory reporting requirements of the industry regulator, Ofgem. The transfer-of-trade was made at book value between two wholly owned subsidiaries of SSE Power Distribution Limited. The balances were transferred as net liabilities of £23.0m, which is a consequence of the Group cash management process which transfers all cash receipts to the ultimate holding company. The Company therefore received cash for assuming these liabilities from S+S Limited, which became part of the Group indebtedness to the Company.

The assets and liabilities acquired were as follows:

	£m
Tangible fixed assets	10.1
Trade debtors	9.2
Accruals and deferred income	(42.3)
	<u>(23.0)</u>

9. Tangible fixed assets

	Distribution assets £m	Other land and buildings £m	Vehicles and miscellaneous equipment £m	Total £m
Cost:				
At 1 April 2011	1,458.8	8.4	71.2	1,538.4
Additions	79.4	-	3.4	82.8
At 31 March 2012	1,538.2	8.4	74.6	1,621.2
Depreciation:				
At 1 April 2011	626.4	1.9	55.2	683.5
Charge for the year	38.6	1.6	0.7	40.9
At 31 March 2012	665.0	3.5	55.9	724.4
Net book value:				
At 31 March 2012	873.2	4.9	18.7	896.8
At 31 March 2011	832.4	6.5	16.0	854.9

	2012	2011
	£m	£m
Tangible fixed assets include:		
Assets in the course of construction	9.3	34.4

Scottish Hydro Electric Power Distribution plc
31 March 2012

**Notes on the Financial statements
for the year ended 31 March 2012**

10. Stocks

	2012 £m	2011 £m
Raw materials and consumables	1.8	1.7
	<u>1.8</u>	<u>1.7</u>

11. Debtors

	2012 £m	2011 £m
Amounts falling due within one year:		
Trade debtors	24.1	20.7
Prepayments and accrued income	27.2	19.0
Amounts owed by group undertakings	405.3	381.0
	<u>456.6</u>	<u>420.7</u>
Amounts falling due after more than one year:		
Amounts owed by group undertakings	22.4	22.4
	<u>479.0</u>	<u>443.1</u>

12. Creditors: amounts falling due within one year

	2012 £m	2011 £m
Short term loans (note 14)	50.0	-
Trade creditors	4.0	4.6
Amounts owed to group undertakings	178.7	78.7
Corporation tax	13.6	17.6
Other creditors	6.9	6.0
Accruals and other deferred income	24.3	37.2
	<u>277.5</u>	<u>144.1</u>

13. Creditors: amounts falling due after more than one year

	2012 £m	2011 £m
Loans (note 14)	143.4	187.7
Loans due to ultimate parent (note 14)	300.0	300.0
Accruals and other deferred income	113.4	87.7
	<u>556.8</u>	<u>575.4</u>

Scottish Hydro Electric Power Distribution plc
31 March 2012

**Notes on the Financial statements
for the year ended 31 March 2012**

14. Analysis of borrowings

	Weighted Average Interest rate 2012 %	Weighted Average Interest rate 2011 %	2012 £m	2011 £m
Within one year				
6.39% European Investment Bank repayable on 24 September 2012	6.39	6.39	50.0	-
Between two and five years				
6.39% European Investment Bank repayable on 24 September 2012	6.39	6.39	-	50.0
Floating rate European Investment Bank repayable on 13 June 2014	1.27	1.04	25.0	25.0
			<u>25.0</u>	<u>75.0</u>
Over five years				
5.90% Loan Stock repayable to SSE plc on 31 March 2022	5.90	5.90	300.0	300.0
1.429% Index linked bond repayable 20 October 2056	1.72	1.43	118.4	112.7
			<u>418.4</u>	<u>412.7</u>
			<u>493.4</u>	<u>487.7</u>

15. Deferred taxation

Deferred taxation is provided as follows:

	2012 £m	2011 £m
Accelerated capital allowances	101.9	111.3
Other timing differences	(1.1)	(2.1)
Hedging reserve	(0.5)	-
Provision for deferred tax	<u>100.3</u>	<u>109.2</u>
		31 March 2012 £m
Provision at 1 April 2011		109.2
Credit to profit and loss account		(9.5)
Charged directly to equity		0.6
Provision at end of year		<u>100.3</u>

16. Share capital

	2012 £m	2011 £m
Authorised:		
62,001,000 ordinary shares of £1 each	62.0	62.0
Allotted, called up and fully paid:		
62,000,000 ordinary shares of £1 each	62.0	62.0

**Notes on the Financial statements
for the year ended 31 March 2012**

17. Reserves

	Hedge Reserve	Profit and loss account	Total
	£m	£m	£m
At 1 April 2011	(1.6)	399.8	398.2
Retained profit for the year	-	58.1	58.1
Dividends	-	(100.0)	(100.0)
Credit in respect of employee share awards	-	0.9	0.9
Gain on effective portion of cash flow hedges (net of tax)	0.1	-	0.1
At 31 March 2012	(1.5)	358.8	357.3

18. Pensions

58% of the Company's employees are members of the Scottish Hydro-Electric Pension Scheme which provides defined benefits based on final pensionable pay. The Company's contributions to this scheme are set in relation to the current service period only (i.e. these are not affected by any surplus or deficit in the scheme relating to past service of its own employees and any other members of the scheme) and as such are accounted for as if they were contributions to a defined contribution scheme.

New employees can opt to join a personal pension scheme which is a money purchase scheme with the Company matching the members' contributions up to a maximum of 6% of salary. That scheme is managed by Friends Provident.

The Company's share of the total contribution payable to the pension schemes during the year was £6.2m (2011 – £5.7m). In addition to this, the Company incurred a further charge, payable to SSE Services plc, of £16.8m (2011 – £16.8m), which related to its share of the Scheme's deficit repair contributions for the year ended 31 March 2012.

The Company has provided a guarantee to the Scottish Hydro Electric Pension Scheme in respect of 80% of the Scheme's deficit. Should the company operating the Scheme, SSE plc, fail to adequately fund the deficit, the Company will provide 80% of the funding required.

19. Employee share-based payments

The majority of the Company's employees are participants in the following Group share schemes:

(i) Savings-related share option schemes ("Sharesave")

This scheme gives employees the option to purchase shares in the parent Company at a discounted market price, subject to them remaining in employment with the Group for the term of the agreement. Employees may opt to save between £5 and £250 per month for a period of 3 or 5 years and at the end of this period, employees have six months to exercise their options by using the cash saved (including a bonus equivalent to interest). If the option is not exercised, the funds may be withdrawn by the employee and the option expires.

(ii) Share Incentive Plan (SIP)

This scheme allows employees the opportunity to purchase shares in the parent Company on a monthly basis. Employees may nominate an amount between £10 and £125 to be deducted from their gross salary. This is then used to purchase shares ('Partnership shares') in the market on the final business day of each month. These shares are then held in trust for a period of 5 years, at which point they are transferred at no further cost to the employee. These shares may be withdrawn at any point during the 5 years, but tax and national insurance would then be payable on any amounts withdrawn.

**Notes on the Financial statements
for the year ended 31 March 2012**

19. Employee share-based payments (continued)

In addition to the shares purchased on behalf of the employee, the Group will also match the purchase up to a maximum of 6 (previously 5) shares ('Matching shares') per month. Again these shares are held in trust for the five years until they are transferred to the employee. If an employee leaves during the first three years, or removes his/her 'partnership' shares, these 'matching' shares are forfeited.

In addition to the above, the following special awards of free shares have been made:

Award made	31 March 2007	31 March 2008
Free shares per employee	20	10
Date at which employee must still be employed to receive award (in addition to 31 March)	30 May 2007	1 August 2008

These awards were made to all employees in recognition of their contribution to the success of the company. Under the arrangements for the awards, the shares will be held in trust for five years, at which point they will be transferred to the employees at no cost to the employee. These shares may be withdrawn at any point during years four and five, but income tax and national insurance would then be payable on any amounts withdrawn.

(iii) Deferred annual incentive scheme

This scheme (previously deferred bonus scheme) applies to senior managers and executive directors of the Group. Under this scheme, 25% of all eligible employees' annual bonus is deferred into shares which only vest after three years, subject to continued service. The number of shares awarded is determined by dividing the relevant pre-tax bonus amount by the share price shortly after the announcement of the results for the financial year to which the bonus relates.

(iv) Performance Share Plan

This scheme applies to Executive Directors and senior executives. The level of these awards are subject to certain performance conditions over the three year performance period, which can be summarised as follows:

Award made		30 June 2009	02 June 2010	02 June 2011
Maximum value of award as a % of base salary		150	150	150
Performance conditions				
Total shareholder return (50% of award) ⁽ⁱ⁾	Full vesting	> 75 th percentile	> 75 th percentile	> 75 th percentile
	25% vesting	median	median	median
Earnings per share (50% of award) ⁽ⁱⁱ⁾	Full vesting	RPI + 9%	RPI + 8%	RPI + 8%
	25% vesting	RPI + 3%	RPI + 2%	RPI + 2%
Dividend per share growth ⁽ⁱⁱⁱ⁾	Full vesting	-	RPI + 6%	RPI + 6%
	25% vesting	-	RPI + 2%	RPI + 2%

These awards will vest after three years to the extent that the relevant performance conditions are met.

⁽ⁱ⁾ Total Shareholder Return (TSR) target relative to other FTSE100 for the 2009 award and Total Shareholder Return (TSR) target relative to other FTSE100 companies and MSCI Europe Utilities Index for all other awards over the relevant performance period. Pro rata vesting will take place between the median and 75th percentile, with no vesting if the minimum target is not met.

⁽ⁱⁱ⁾ Under the EPS performance condition, pro rata vesting between the lower and upper level above RPI, with no vesting if the minimum EPS growth target is not achieved.

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19. Employee share-based payments (continued)

⁽ⁱⁱⁱ⁾ Under the Dividend per share growth performance condition, pro rata vesting between 2% and 6% above RPI, with no vesting if the minimum dividend per share growth target is not achieved.

Details used in the calculation of these costs are as follows:

(i) Savings-related share option scheme

As at 31 March 2012

Award Date	Option Price (pence)	Outstanding at start of year	Granted	Exercised	Lapsed	Outstanding at end of year	Date from which exercisable	Expiry date
14 July 2005	886	21,688		(746)	(20,942)	-	1 October 2010	31 March 2011
11 July 2006	999	61,366		(46,510)	(161)	14,695	1 October 2011	31 March 2012
10 July 2007	1,306	16,945		-	(16,945)	-	1 October 2010	31 March 2011
10 July 2007	1,306	35,796		-	(500)	35,296	1 October 2012	31 March 2013
17 July 2008	1,274	9,823		(5,578)	(30)	4,215	1 October 2011	31 March 2012
17 July 2008	1,274	28,270		-	(1,148)	27,122	1 October 2013	31 March 2014
30 June 2009	1,042	16,497		-	(867)	15,630	1 October 2012	31 March 2013
30 June 2009	1,042	58,862		-	(1,758)	57,104	1 October 2014	31 March 2015
30 June 2010	871	51,661		-	(2,291)	49,370	1 October 2013	31 March 2014
30 June 2010	871	327,071		-	(9,925)	317,146	1 October 2015	31 March 2016
28 June 2011	1,105	-	19,417	-	(326)	19,091	1 October 2014	31 March 2015
28 June 2011	1,105	-	61,973	-	(753)	61,220	1 October 2016	31 March 2017
		627,979	81,390	(52,834)	(55,646)	600,889		

As at 31 March 2011

Award Date	Option Price (pence)	Outstanding at start of year	Outstanding transferred in	Granted	Exercised	Lapsed	Outstanding at end of year	Date from which exercisable	Expiry date
16 July 2004	622	210	-	-	-	(210)	-	1 October 2009	31 March 2010
14 July 2005	886	119,071	2,262	-	(98,489)	(1,156)	21,688	1 October 2010	31 March 2011
11 July 2006	999	374	-	-	(374)	-	-	1 October 2009	31 March 2010
11 July 2006	999	64,862	496	-	-	(3,992)	61,366	1 October 2011	31 March 2012
10 July 2007	1,306	19,885	156	-	-	(3,096)	16,945	1 October 2010	31 March 2011
10 July 2007	1,306	60,649	651	-	-	(25,504)	35,796	1 October 2012	31 March 2013
17 July 2008	1,274	16,751	259	-	-	(7,187)	9,823	1 October 2011	31 March 2012
17 July 2008	1,274	50,927	750	-	-	(23,407)	28,270	1 October 2013	31 March 2014
30 June 2009	1,042	32,209	1,739	-	-	(17,451)	16,497	1 October 2012	31 March 2013
30 June 2009	1,042	139,348	1,568	-	-	(82,054)	58,862	1 October 2014	31 March 2015
30 June 2010	871	-	-	55,230	-	(3,569)	51,661	1 October 2013	31 March 2014
30 June 2010	871	-	-	329,516	-	(2,445)	327,071	1 October 2015	31 March 2016
		504,286	7,881	384,746	(98,863)	(170,071)	627,979		

As share options are exercised continuously throughout the period from 1 October to 31 March, the weighted average share price during this period of 1,291p (2011: 1,177p) is considered representative of the weighted average share price at the date of exercise. The weighted average share price of forfeitures is simply the option price to which the forfeit relates.

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19. Employee share-based payments (continued)

The fair value of these shares at vesting, calculated using the Black-Scholes model, and the assumptions made in that model are as follows:

	July 2006		July 2007		July 2008		June 2009		June 2010		June 2011	
	3 Year	5 Year	3 Year	5 Year	3 Year	5 Year	3 Year	5 Year	3 Year	5 Year	3 Year	5 Year
Fair value of option	217p	227p	287p	313p	304p	339p	244p	269p	231p	246p	171p	163p
Expected volatility	19%	19%	25%	25%	28%	28%	35%	35%	19%	19%	18%	18%
Risk free rate	4.7%	4.7%	5.8%	5.7%	4.9%	5.0%	2.7%	2.9%	1.4%	2.2%	1.2%	2.1%
Expected dividends	4.8%	4.8%	5.3%	5.2%	4.1%	4.2%	4.1%	4.2%	1.7%	2.2%	6.1%	6.1%
Term of the option	3 yrs	5 yrs	3 yrs	5 yrs	3 yrs	5 yrs	3 yrs	5 yrs	3 yrs	5yrs	3yrs	5yrs
Underlying price at grant date	1,180p	1,180p	1,460p	1,460p	1,397p	1,397p	1,139p	1,139p	1,089p	1,089p	1,393p	1,393p
Strike price	999p	999p	1,306p	1,306p	1,274p	1,274p	1,042p	1,042p	871p	871p	1,105p	1,105p

Expected price volatility was obtained by calculating the historical volatility of the Group's share price over the previous 12 months.

ii) Share Incentive Plan

Matching shares

	2012		2011	
	Shares	Weighted average price (pence)	Shares	Weighted average price (pence)
Outstanding at start of year	142,861	1,133	172,914	1,134
Outstanding transferred in	-	-	4,683	957
Granted	34,768	1,315	39,354	1,161
Forfeited	(2,361)	1,194	(3,310)	1,215
Exercised	(3,671)	1,310	(11,662)	1,149
Transferred to pool	(19,694)	1,328	(59,118)	1,149
Outstanding at end of year	151,903	1,144	142,861	1,133
Exercisable at end of year	60,761	1,144	81,817	1,060

When shares have been held for a period of 5 years they are transferred to a pooled share account. At this point the holder has an unconditional right to the share but has chosen not to exercise immediately.

The fair value of these shares is not subject to valuation using the Black-Scholes model. However, the fair value of shares granted in the year is equal to the weighted average price paid for the shares at the grant date as shares are acquired out of the market as at that date to satisfy awards made under the scheme.

As share options are exercised continuously throughout the year, the weighted average share price during this period of 1,310p (2011: 1,149p) is considered representative of the weighted average share price at the date of exercise.

Shares purchased under this scheme prior to 7 November 2002 have not been included as permitted by the transitional rules under FRS 20.

**Notes on the Financial statements
for the year ended 31 March 2012**

19. Employee share-based payments (continued)

Free shares

	2012		2011	
	Shares	Weighted average price (pence)	Shares	Weighted average price (pence)
Outstanding at start of year	17,751	1,163	53,567	1,160
Outstanding transferred in	-	-	1,020	1,212
Forfeited	(20)	1,408	(140)	1,210
Exercised	(210)	1,310	(7,294)	1,149
Transferred to pool	-	-	(29,402)	1,000
Outstanding at end of year	17,521	1,161	17,751	1,163
Exercisable at end of year	17,521	1,161	17,751	1,163

The fair value of these shares is not subject to valuation using the Black-Scholes model. However, the fair value of shares granted in the year is equal to the weighted average price paid for the shares at the grant date as shares are acquired out of the market as at that date to satisfy awards made under the scheme.

As share options are exercised continuously throughout the year, the weighted average share price during this period of 1,310p (2011: 1,149p) is considered representative of the weighted average share price at the date of exercise.

(iii) Deferred annual incentive scheme

	2012		2011	
	Shares	Price (pence)	Shares	Price (pence)
Outstanding at start of year	17,655	1,126	11,337	1,152
Granted	4,715	1,342	6,318	1,079
Exercised	(5,174)	1,545	-	-
Outstanding at end of year	17,196	1,059	17,655	1,126
Exercisable at end of year	-	-	-	-

The fair value of these shares is not subject to valuation using the Black-Scholes model. However, the fair value of shares granted in the year is equal to the weighted average price paid for the shares at the grant date as shares are acquired in the market as at that date to satisfy awards made under the scheme.

(iv) Performance Share Plan

	2012		2011	
	Shares	Price (pence)	Shares	Price (pence)
Outstanding at start of year	82,765	1,239	56,504	1,369
Granted	30,409	1,342	39,990	1,079
Forfeited	(16,016)	1,545	(11,505)	1,353
Exercised	(3,171)	1,545	(2,224)	1,076
Outstanding at end of year	93,987	1,210	82,765	1,239

Of the outstanding options at the end of the year, none were exercisable.

The fair value of the performance share plan shares is not subject to valuation using the Black-Scholes model. The fair value of shares granted in the year is equal to the closing market price on the date of grant.

**Notes on the Financial statements
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20. Derivatives and financial instruments

Exposure to interest rate risk arises in the normal course of the Company's business. Derivative financial instruments are entered into to hedge exposure to risk. The objectives and policies for holding or issuing financial instruments and similar contracts, and the strategies for achieving those objectives that have been followed during the year are explained below. The Group's Risk and Trading Committee, a standing committee of the Management Board, comprising three executive directors and senior managers from the Generation and Supply and Finance functions, oversees the control of these activities. This committee is discussed further in the Annual Report of the ultimate parent, SSE plc.

The Group's treasury department is responsible for managing the banking and liquidity requirements of the Company, 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 Group's Management Board and any breaches of these policies are reported to the Risk and Trading Committee and Group's Audit Committee.

(i) Risk

Interest rate risk

Interest rate risk derives from the Company's exposure to changes in value of an asset or liability or future cash flows through changes in interest rates.

The Company's policy is to manage this risk by stipulating that a minimum of 50% of borrowings be subject to fixed rates of interest, either directly through the debt instruments themselves or through the use of derivative financial instruments. Such instruments include interest rate swaps and options, forward rate agreements and, in the case of debt raised in currencies other than sterling, cross currency swaps.

Although interest rate derivatives are primarily used to hedge risk relating to current borrowings, under certain circumstances they may also be used to hedge future borrowings. Any such pre-hedging is unwound at the time of pricing the underlying debt, either through cash settlement on a net present value basis or by transacting offsetting trades. The floating rate borrowings mainly comprise commercial paper issued at interest rates less than LIBOR and cash advances from the European Investment Bank (EIB).

Effective interest rate analysis

In respect of income earning financial assets and interest bearing financial liabilities, the following table indicates their effective interest rates as at the balance sheet date and the periods in which they re-price or mature:

At 31 March 2012	Effective interest rate %	Total £m	Within 1 year £m	1-2 years £m	2-5 years £m	More than 5 years £m
Long term bonds	1.7183	118.4	-	-	-	118.4
Other bank loans – fixed	5.9700	350.0	50.0	-	-	300.0
Other bank loans – floating	1.2690	25.0	-	-	25.0	-
Interest rate swaps – fixed	4.9164	75.0	-	-	-	75.0

(ii) Fair values

The fair values of the Company's financial assets and financial derivatives, and the carrying amounts in the balance sheet are analysed below. Balances included in the analysis of primary financial assets and liabilities include cash and cash equivalents, loans and borrowings, trade and other debtors, trade and other creditors and provisions, all of which are disclosed separately. Own use commodity contracts are not considered to be financial instruments.

**Notes on the Financial statements
for the year ended 31 March 2012**

20. Derivatives and financial instruments (continued)

Summary fair values

The fair values of the primary financial assets and liabilities together with their carrying values are as follows:

	2012 Carrying Value £m	2012 Fair Value £m	2011 Carrying Value £m	2011 Fair Value £m
Financial Assets				
Trade and other debtors	451.8	451.8	424.1	424.1
Financial Liabilities				
Trade and other creditors	207.1	207.1	107.8	107.8
Bank loans and overdrafts	75.0	76.1	75.0	78.2
Long-term bonds	118.4	120.4	112.7	115.8
Loan Stock	300.0	367.9	300.0	322.9
Derivative financial liabilities	23.7	23.7	10.8	10.8

Fair values have been determined with reference to closing market prices.

Unless otherwise stated, carrying value approximates fair value.

Financial derivative instruments – disclosure

For disclosure purposes, derivative financial instruments are classified into two categories, operating derivatives and financing derivatives. The company only utilise financing derivatives. Financing derivatives include all fair value and cash flow interest rate hedges, non-hedge accounted (mark-to-market, noted as MTM) interest rate derivatives, cash flow foreign exchange hedges and non-hedge accounted (MTM) foreign exchange contracts. Non-hedge accounted contracts are treated as held for trading (MTM). The carrying value is the same as the fair value for all instruments. All balances are stated gross of associated deferred taxation.

The net financial liabilities of £23.7m (2011 - £10.8m) are represented as creditors that are due after more than one year.

Basis of determining fair value

Closing rate market values have been used to determine the fair values of the interest rate and foreign currency contracts and denominated long-term fixed rate debt. Estimates applied reflect the management's best estimates of these factors.

21. Commitments and contingencies

(i) Capital expenditure

	2012 £m	2011 £m
Contracted for but not provided	6.5	11.3

(ii) Operating lease commitments

Leases as lessee:

	2012 £m	2011 £m
Amount included in the profit and loss account relating to the current year leasing arrangements	0.5	0.5

**Notes on the Financial Statements
for the year ended 31 March 2012**

21. Commitments and contingencies (continued)

(ii) Operating lease commitments (continued)

The payments under operating leases which are due to be made in the next year, analysed over the periods when the leases expire, are:

	Other assets	
	2012	2011
	£m	£m
Less than one year	0.1	-
Between two and five years	0.3	0.4
After five years	0.1	0.1
	<u>0.5</u>	<u>0.5</u>

(iii) Guarantees and Indemnities

The Company has provided a guarantee in relation to £300.0m Eurobonds held by SSE plc. This Guarantee has been jointly provided with Scottish Hydro Electric Transmission Limited.

22. Reconciliation of operating profit to operating cashflows

	2012	2011
	£m	£m
Reconciliation of operating profit to operating cash flows		
Operating profit including gains on disposals	101.7	103.7
Depreciation	40.9	39.6
Customer contributions and capital grants released	(3.4)	(3.4)
Increase in stocks	(0.1)	(0.3)
Increase in debtors	(11.6)	(4.0)
Increase/(decrease) in creditors	15.2	9.9
Movement in intercompany	75.7	(45.0)
Charge in respect of employee share awards	0.9	0.9
Net cash inflow from operating activities	<u>219.3</u>	<u>101.4</u>

23. Net debt

Reconciliation of net cash flow to movement in net debt

	2012	2011
	£m	£m
Cash inflow/(outflow) from increase/(decrease) in cash ⁽ⁱ⁾	-	-
Cash (inflow)/outflow from (increase)/decrease in debt and lease financing	-	-
Other movement	(5.7)	(5.1)
Movement in net debt in the year	<u>(5.7)</u>	<u>(5.1)</u>
Net debt at 1 April	(487.7)	(482.6)
Net debt at 31 March	<u>(493.4)</u>	<u>(487.7)</u>

**Notes on the Financial Statements
for the year ended 31 March 2012**

23. Net debt (continued)

Analysis of net debt

	As at 1 April 2011 £m	Increase in cash ⁽ⁱ⁾ £m	Increase in debt £m	Non-cash movements ⁽ⁱⁱ⁾ £m	As at 31 March 2012 £m
Cash at bank and in hand	-	-	-	-	-
Net borrowings due within one year	-	-	(50.0)	-	(50.0)
Net borrowings due after more than one year	(487.7)	-	50.0	(5.7)	(443.4)
Net debt	(487.7)	-	-	(5.7)	(493.4)

(i) The Company does not hold cash balances at any time. Cash generated or required by the Company is remitted to or obtained from SSE plc or SSE Services plc. As a result the movement in indebtedness from the Group (reflected in movement in debtor and creditor balances on the balance sheet) can be said to represent the cash generated in the year.

(ii) The fair value adjustment relates to the adoption of FRS 26 from 1 April 2005 and is in relation to certain hedged debt balances, which are fair valued in accordance with the fair value hedge accounting requirements under the standard. The Company's policies are explained in the Notes to the Financial statements. Movements in these values are shown as a non-cash item in the analysis of net debt.

24. Ultimate parent company

The Company is a subsidiary of SSE plc, which is the ultimate parent company and is registered in Scotland. The largest and smallest group in which the results of the Company are consolidated is that headed by SSE plc. The consolidated financial statements of the group (which include those of the Company) are available from Corporate Communications, Inveralmond House, 200 Dunkeld Road, Perth PH1 3AQ.