

Registered number: 3600574

WESTERN POWER DISTRIBUTION (WEST MIDLANDS) plc

ANNUAL REPORT AND FINANCIAL STATEMENTS

For the year ended 31 March 2019



Western Power Distribution (West Midlands) plc

Contents

	Page
Strategic report	1
Director's report	25
Directors' responsibilities statement	28
Independent auditor's report to the members of Western Power Distribution (West Midlands) plc	29
Financial statements:	
Profit and loss account	35
Statement of comprehensive income	36
Statement of changes in equity	37
Balance sheet	38
Statement of cash flows	39
Notes to the financial statements	40

Strategic report

For the year ended 31 March 2019

The directors present their report and the audited financial statements of Western Power Distribution (West Midlands) plc (the "Company" or "WPD West Midlands"), company number 3600574, for the year ended 31 March 2019.

Ownership

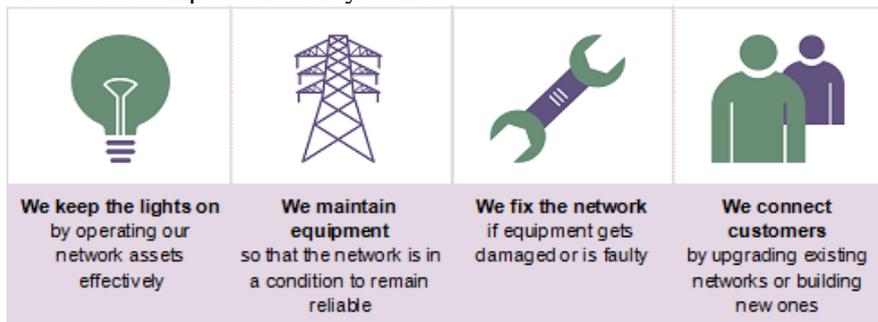
WPD West Midlands is owned by Western Power Distribution plc, which is a public limited company owned by one shareholder, PPL Corporation. PPL Corporation is an electricity utility based in Allentown, Pennsylvania, United States of America.

Business model

WPD West Midlands is an electricity Distribution Network Operator ("DNO"), delivering electricity to approximately 2.5 million customers over an area of 13,300 square kilometres in the West Midlands of England and employing over 2,000 staff.

The 2.5 million customers are registered with licensed electricity suppliers, who in turn pay WPD West Midlands for distributing electricity across its network. Our costs are regulated and make up around 17% of a domestic customer's bill, which they pay to their supplier.

What we do comprises four key tasks:



WPD West Midlands' network comprises approximately 23,000 km of overhead lines, 41,000 km of underground cable and 51,000 transformers. In 2018/19 WPD West Midlands distributed 4,449 megawatts of electricity.

Group background

Western Power Distribution plc is the parent of a group ("WPD Group" or "WPD") whose principal operating activity is conducted by the four DNOs; Western Power Distribution (South West) plc ("WPD South West"), Western Power Distribution (South Wales) plc ("WPD South Wales"), Western Power Distribution (East Midlands) plc ("WPD East Midlands"), and Western Power Distribution (West Midlands) plc ("WPD West Midlands"). Where appropriate the four DNOs share engineering control and other systems.

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

Regulation

WPD West Midlands is a monopoly regulated by the Gas and Electricity Markets Authority, which operates through Ofgem.

Strategic report (continued)

For the year ended 31 March 2019

Regulation (continued)

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:

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

The operations are regulated under the distribution licence which sets the requirements that WPD West Midlands 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 WPD West Midlands is 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.

The WPD Group 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 Group DNOs, ahead of the other five licensed distributor groups. WPD Group's modified licences took effect from 1 April 2015.

Our RIIO-ED1 business plan is available as 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 the Company 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 the Company to predict investment requirements into the long term. The Company 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 plan to build on our Future Networks Programme and invest approximately £73m up to 2023 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.

Strategic report (continued)

For the year ended 31 March 2019

Long term strategy (continued)

- Adapting to change (continued)

On flexibility our Flexible Power product has transitioned to business as usual with two tender rounds per annum. Our last round contracted with 28 megawatts of flexibility. Our next (third) round is seeking 93.4 megawatts of flexibility required to operate over the summer and winter of 2019 and affects over £25m of reinforcements.

WPD leads on the Electricity Networks Association (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.

- Investment 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.

Safety

Safety is the most important priority at WPD West Midlands. The Company continuously promotes safety, both within the business and also externally to groups such as school children, land owners and construction operators.

There are robust safety policies in place that are designed based on the assessment of the hazards and risks involved with a particular activity and are further developed in response to incidents that have occurred both in WPD and other businesses, and to changes in legislations.

WPD West Midlands' safety management system is compliant with the requirements of British Standard, OHSAS 18001 (Occupational Health and Safety Assessment Series) and we continuously looks for opportunities to enhance safety. The staff play an active role in many national committees and steering groups which concentrate on the future of safety and training policies 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:

<https://www.westernpower.co.uk/customers-and-community/health-safety>

Strategic report (continued)

For the year ended 31 March 2019

Key goals (continued)

Network performance & security

WPD West Midlands is committed to providing a secure, reliable and continuous network connection to its customers. It looks at the physical security aspects of the network and at preventing any cyber breach incidents. WPD West Midlands recognises that its 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 West Midlands. 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 West Midlands is dedicated to conducting its business as a responsible steward of the environment. The Company monitors its impact in terms of carbon footprint, waste recycling and fluid loss.

Every member of staff is made aware of the Company'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.

More detailed information on our environmental goal could be found in our published report available at:

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

Stakeholder value and 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 look towards future stakeholders. 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 West Midlands strongly believes that customer satisfaction is the key to the future success of the business. The Company 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.

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 a number of locations across WPD every year and stringently assesses WPD's engagement activities, including delivery, timeliness, information, professionalism and staff attitudes, every year.

Customer awareness is a key commitment for WPD West Midlands and we engage in ongoing communications so that the Company'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.

Strategic report (continued)

For the year ended 31 March 2019

Key goals (continued)

Stakeholder value and engagement (continued)

- Employees

Our business is built by our people and WPD West Midlands is fully committed to keeping its employees motivated and actively involved. Equality of opportunity is key to WPD West Midlands' approach to hiring, training and promoting employees. WPD West Midlands 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 West Midlands 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.

In order to help inform a range of stakeholders on how WPD earns and spends its allowed revenue, WPD became the first DNO to voluntarily publish its RIIO accounts in 2018. The aim of the accounts is to demonstrate where WPD is investing in its networks and clearly shows the returns our investors receive. Our work on RIIO accounts has been extremely useful on discussions, about the level of returns made by DNOs, with the likes of Citizen's Advice and other Government bodies. The RIIO accounts work underpins Ofgem's latest RIIO reporting framework, Regulatory Financial Performance Reporting ("RFPR") due for publication later this year.

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

- WPD's CEO & Senior Managers attend national groups such as 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 monitor areas such as pollution prevention, habitat conservation and other matters relating to protection and enhancement of environment. WPD continuously works together with the EA to improve its environmental performance.

Strategic report (continued)

For the year ended 31 March 2019

Key goals (continued)

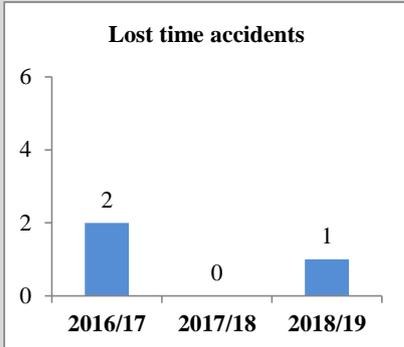
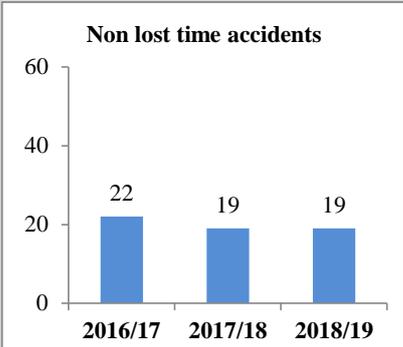
Stakeholder value and engagement (continued)

- Shareholder

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

Key performance indicators (KPIs)

KPIs are used to assess progress against the overall strategy and key goals.

	KPI	Performance and comments																
Safety	Accident rate	<div style="display: flex; justify-content: space-around;"> <div style="text-align: center;">  <p>Lost time accidents</p> <table border="1"> <tr><th>Year</th><th>Count</th></tr> <tr><td>2016/17</td><td>2</td></tr> <tr><td>2017/18</td><td>0</td></tr> <tr><td>2018/19</td><td>1</td></tr> </table> </div> <div style="text-align: center;">  <p>Non lost time accidents</p> <table border="1"> <tr><th>Year</th><th>Count</th></tr> <tr><td>2016/17</td><td>22</td></tr> <tr><td>2017/18</td><td>19</td></tr> <tr><td>2018/19</td><td>19</td></tr> </table> </div> </div> <p>The total number of accidents to staff increased from 19 in 2017/18 to 20 in 2018/19. Electricity distribution carries inherent safety risks, the 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.</p> <p>In addition WPD monitors the overall rate of accident per 100 employees (as reported to Ofgem). The accident rate for WPD Group for 2018/19 is 0.86 (2017/18: 0.87), outperforming the RIIO-ED1 target of 1.6 (a reduction of 10% over price control prior to RIIO-ED1). Further details on our performance reporting to Ofgem regarding safety can be found at the link below:</p> <p>https://www.westernpower.co.uk/customers-and-community/performance-reporting-riio-ed1/safety</p>	Year	Count	2016/17	2	2017/18	0	2018/19	1	Year	Count	2016/17	22	2017/18	19	2018/19	19
Year	Count																	
2016/17	2																	
2017/18	0																	
2018/19	1																	
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Network performance & security	Customer minutes lost (CML)	<div style="text-align: center;">  <p>CML</p> <table border="1"> <tr><th>Year</th><th>Target CML</th><th>Actual CML</th></tr> <tr><td>2016/17</td><td>53.6</td><td>32</td></tr> <tr><td>2017/18</td><td>53</td><td>22.5</td></tr> <tr><td>2018/19</td><td>52.8</td><td>32.3</td></tr> </table> </div> <p>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 the Company is performing better than its targets as we are focused on ensuring complete network reliability for our customers.</p>	Year	Target CML	Actual CML	2016/17	53.6	32	2017/18	53	22.5	2018/19	52.8	32.3				
Year	Target CML	Actual CML																
2016/17	53.6	32																
2017/18	53	22.5																
2018/19	52.8	32.3																

Strategic report (continued)

For the year ended 31 March 2019

Key performance indicators (KPIs) (continued)

	KPI	Performance and comments													
Network performance & security	Number of customer interruptions (CI)	<table border="1"> <caption>CI</caption> <thead> <tr> <th>Year</th> <th>Target CI</th> <th>Actual CI</th> </tr> </thead> <tbody> <tr> <td>2016/17</td> <td>87.1</td> <td>59</td> </tr> <tr> <td>2017/18</td> <td>85.4</td> <td>47.4</td> </tr> <tr> <td>2018/19</td> <td>84.1</td> <td>55.36</td> </tr> </tbody> </table>		Year	Target CI	Actual CI	2016/17	87.1	59	2017/18	85.4	47.4	2018/19	84.1	55.36
	Year	Target CI	Actual CI												
2016/17	87.1	59													
2017/18	85.4	47.4													
2018/19	84.1	55.36													
Other measures (WPD Group)	<p>- In 2018/19 88.01% (2017/18: 88.5%) of customers had their power restored within an hour of a high voltage fault, the target being 87.5% (2017/18: 85%).</p> <p>- 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 26 (2017/18: 52), an improvement of over 99% on our 2012/13 benchmark performance. Customers received a set payment where we failed to achieve the GSOP.</p>														
Financial stability	Revenue	2018/19 (£m) <hr/> 524.6	2017/18 (£m) <hr/> 496.7												
	Profit before taxation (PBT)	2018/19 (£m) <hr/> 236.7	2017/18 (£m) <hr/> 224.6												

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. Year on year the Company is performing better than its targets as we are focused on ensuring complete network reliability for our customers.

The majority of WPD West Midlands' revenue is fixed across the current price control period. Ofgem sets the revenues at a level that covers reasonable costs and allows a reasonable rate of return. In addition to the base level of revenue that a DNO can earn, there are incentive measures including customer service outputs, network outputs and innovation, which constitute allowed revenue.

As part of regulatory process, Ofgem sets the allowed rate of return within each price control, which for RIIO-ED1 is set at 6.4%. As evident from the level of capital expenditure below, WPD West Midlands 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.

Strategic report (continued)

For the year ended 31 March 2019

Key performance indicators (KPIs) (continued)

	KPI	Performance and comments		
Financial stability	Fixed asset additions	2018/19	2017/18	<p>WPD West Midlands 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 RII0-ED1 period to date we have invested £1.1bn in capital related activities.</p>
	Tangible fixed asset additions	243.6	287.9	
	Regulatory asset value (RAV)	2018/19	2017/18	<p>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 DNO's with respect to impairment calculations are calculated using RAV.</p> <p>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.</p>
		2,452.0	2,365.1	
	Gearing	2018/19	2017/18	<p>Gearing for the Company 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 the internal KPI, the gearing ratio for WPD West Midlands does not exceed 65%.</p>
	Net debt*	1,467.2	1,494.8	
	RAV	2,452.0	2,365.1	
	Net debt to RAV	59.8%	63.2%	
	*Refer to note 18 on page 63 for calculation of net debt			

Strategic report (continued)

For the year ended 31 March 2019

Key performance indicators (KPIs) (continued)

		KPI	Performance and comments																	
Financial stability	Interest cover	2018/19	2017/18	A minimum ratio of earnings before interest, tax, depreciation and amortisation ("EBITDA") to interest payable is required by credit facility covenants for the Company. It is also used as a key internal indicator of the financial health of the DNO. 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 sufficient level of earnings to cover interest payments.																
		(£m)	(£m)																	
	PBT	236.7	224.6																	
	Interest payable	78.4	77.7																	
	Depreciation	68.7	66.7																	
	Amortisation-intangible assets	0.8	0.5																	
	Amortisation-customer contributions	(13.3)	(12.8)																	
	Earnings before interest, tax, depreciation and amortisation ("EBITDA")	371.3	356.7																	
Interest payable	78.4	77.7																		
	Interest cover	4.7	4.6																	
Environment	Business carbon footprint ("BCF")	<div style="text-align: center;"> <p>tCO₂e - measure for BCF</p> <table border="1" style="margin: 0 auto;"> <thead> <tr> <th>Year</th> <th>tCO₂e</th> </tr> </thead> <tbody> <tr> <td>2012/13</td> <td>23,831</td> </tr> <tr> <td>2013/14</td> <td>21,004</td> </tr> <tr> <td>2014/15</td> <td>23,060</td> </tr> <tr> <td>2015/16</td> <td>23,753</td> </tr> <tr> <td>2016/17</td> <td>22,048</td> </tr> <tr> <td>2017/18</td> <td>18,916</td> </tr> <tr> <td>2018/19</td> <td>21,794</td> </tr> </tbody> </table> </div>			Year	tCO ₂ e	2012/13	23,831	2013/14	21,004	2014/15	23,060	2015/16	23,753	2016/17	22,048	2017/18	18,916	2018/19	21,794
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2018/19	21,794																			
	<p>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"). WPD South West follows a recognised methodology as described within international business carbon footprint standards, the Greenhouse Gas ("GHG") reporting protocol and ISO14064-1.</p> <p>WPD's current target is a 5% reduction over the RIIO-ED1 period based on the baseline year of 2012/13. At 2018/19 WPD Group is outperforming the target.</p> <p>For further details on various elements that make up our BCF refer to our detailed environment report at the below link:</p> <p>https://www.westernpower.co.uk/customers-and-community/environment</p>																			

Strategic report (continued)

For the year ended 31 March 2019

Key performance indicators (KPIs) (continued)

KPI	Performance and comments																					
<p style="writing-mode: vertical-rl; transform: rotate(180deg);">Environment</p> <p>SF6 emissions (emissions as % of SF6 bank)</p>	<p>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.</p> <p>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.</p> <div data-bbox="635 698 1461 1227"> <table border="1"> <caption>SF6 % Leakage</caption> <thead> <tr> <th>Year</th> <th>Actual % leakage</th> <th>Target % leakage</th> </tr> </thead> <tbody> <tr> <td>2013/14</td> <td>0.54%</td> <td>0.38%</td> </tr> <tr> <td>2014/15</td> <td>0.32%</td> <td>0.38%</td> </tr> <tr> <td>2015/16</td> <td>0.78%</td> <td>0.38%</td> </tr> <tr> <td>2016/17</td> <td>0.23%</td> <td>0.38%</td> </tr> <tr> <td>2017/18</td> <td>0.76%</td> <td>0.38%</td> </tr> <tr> <td>2018/19</td> <td>0.02%</td> <td>0.38%</td> </tr> </tbody> </table> </div> <p>Overall the level of leakage is reducing over time as older units are replaced with new units which also contain lower levels of SF6. 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.</p>	Year	Actual % leakage	Target % leakage	2013/14	0.54%	0.38%	2014/15	0.32%	0.38%	2015/16	0.78%	0.38%	2016/17	0.23%	0.38%	2017/18	0.76%	0.38%	2018/19	0.02%	0.38%
Year	Actual % leakage	Target % leakage																				
2013/14	0.54%	0.38%																				
2014/15	0.32%	0.38%																				
2015/16	0.78%	0.38%																				
2016/17	0.23%	0.38%																				
2017/18	0.76%	0.38%																				
2018/19	0.02%	0.38%																				

Strategic report (continued)

For the year ended 31 March 2019

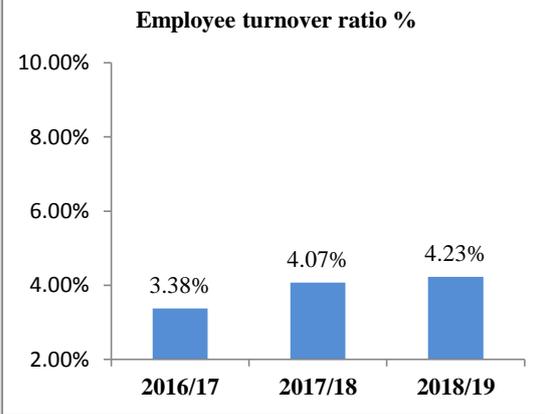
Key performance indicators (KPIs) (continued)

KPI	Performance and comments															
Environment	<p>Fluid cable losses</p>															
	<p>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 West Midlands works to an operating code agreed with the Environment Agency, and assesses both the condition and the environmental risk posed by the fluid filled cables which the Company owns.</p> <div data-bbox="643 730 1449 1189"> <table border="1"> <caption>Losses in litres</caption> <thead> <tr> <th>Year</th> <th>Actual losses (litres)</th> </tr> </thead> <tbody> <tr> <td>2012/13</td> <td>13,917</td> </tr> <tr> <td>2013/14</td> <td>10,556</td> </tr> <tr> <td>2014/15</td> <td>16,660</td> </tr> <tr> <td>2015/16</td> <td>5,791</td> </tr> <tr> <td>2016/17</td> <td>9,421</td> </tr> <tr> <td>2017/18</td> <td>12,771</td> </tr> <tr> <td>2018/19</td> <td>31,474</td> </tr> </tbody> </table> </div> <p>The losses from WPD West Midlands' 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. In the current year, the WPD Group has improved its technique for detection of losses as well as introduced a better system for loss reporting. This has resulted in higher losses detected and reported in the current year as compared to previous years. In addition, an increase in losses is also attributed to prolonged hot dry spells in May to August 2018 which affected the ground conditions and compromised the cable integrity.</p>	Year	Actual losses (litres)	2012/13	13,917	2013/14	10,556	2014/15	16,660	2015/16	5,791	2016/17	9,421	2017/18	12,771	2018/19
Year	Actual losses (litres)															
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2015/16	5,791															
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2017/18	12,771															
2018/19	31,474															
<p>Other measures</p>	<p><u>Environmental management standard</u></p> <p>In May 2017, WPD West Midlands gained certification to the new ISO14001:2015 environmental management standard. The latest six monthly surveillance audits were undertaken in April and November 2018 with no major non-conformances raised.</p>															

Strategic report (continued)

For the year ended 31 March 2019

Key performance indicators (KPIs) (continued)

KPI	Performance and comments
<i>Customers</i>	
Overall customer satisfaction (WPD Group)	 <p>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. For WPD's four licence areas around 22,000 customers are surveyed per year. For the regulatory year 2018/19, the WPD Group has been rated the number one DNO for customer satisfaction for the eighth consecutive year.</p> <p>Ofgem also compared the speed of response that a DNO call centre provides and the WPD Group is consistently identified as the top performer with an average speed of response below 1.58 seconds.</p>
Stakeholder engagement incentive	<p>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 2017/18 WPD was again rated first place in the industry (outperforming every DNO, gas and transmission network) with a score of 8.75 (2016/17: 8.53) out of 10. This was worth £6.72m (17/18 prices) and will be applied to 2019/20 revenues across the four DNOs. WPD entered three written submissions, hosted a one day audit of the Consumer Vulnerability part of the submission and this was then followed by a question and answer session with an Ofgem-appointed judging panel of experts.</p>
<i>Employees</i>	
Employee turnover ratio (WPD Group)	 <p>The turnover ratio includes retirements and the reason for a slight increase year on year is due to more employees reaching the retirement stage. On an overall basis, the Company has a very low employee turnover ratio, an indication of high levels of satisfaction and motivation of staff.</p>

Stakeholder value & engagement

Strategic report (continued)

For the year ended 31 March 2019

Key Performance Indicators (KPIs) (continued)

KPI	Performance and comments													
Stakeholder value & engagement	<p><i>Employees (continued)</i></p> <p>Gender pay gap (WPD Group)</p>	<div style="display: flex; justify-content: space-around;"> <div data-bbox="632 454 1038 786"> <p style="text-align: center;">Mean hourly pay gap %</p> <table border="1"> <caption>Mean hourly pay gap %</caption> <thead> <tr> <th>Year</th> <th>Mean hourly pay gap %</th> </tr> </thead> <tbody> <tr> <td>2016/17</td> <td>9%</td> </tr> <tr> <td>2017/18</td> <td>8.70%</td> </tr> </tbody> </table> </div> <div data-bbox="1062 454 1469 786"> <p style="text-align: center;">Median hourly pay gap %</p> <table border="1"> <caption>Median hourly pay gap %</caption> <thead> <tr> <th>Year</th> <th>Median hourly pay gap %</th> </tr> </thead> <tbody> <tr> <td>2016/17</td> <td>10.5%</td> </tr> <tr> <td>2017/18</td> <td>9.60%</td> </tr> </tbody> </table> </div> </div> <p>WPD’s median gender pay gap for the year ended 31 March 2018 is 8.3% below the national gender gap and 17.9% 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. This is based on the latest available data.</p> <p>Further information about WPD gender pay gap could be found at: https://www.westernpower.co.uk/useful-documents</p>	Year	Mean hourly pay gap %	2016/17	9%	2017/18	8.70%	Year	Median hourly pay gap %	2016/17	10.5%	2017/18	9.60%
	Year	Mean hourly pay gap %												
	2016/17	9%												
	2017/18	8.70%												
Year	Median hourly pay gap %													
2016/17	10.5%													
2017/18	9.60%													
<p>Other measures (WPD Group)</p>	<p><u><i>Employee satisfaction</i></u></p> <p>WPD’s 2018 staff survey was distributed to all staff. 84% of those who participated believe WPD is a good place to work.</p>													
<p><i>Suppliers</i></p> <p>Payment performance</p>	<div style="display: flex;"> <div data-bbox="632 1267 1038 1671" style="flex: 1;"> <p style="text-align: center;">Average no. of payment days</p> <table border="1"> <caption>Average no. of payment days</caption> <thead> <tr> <th>Period</th> <th>Average no. of payment days</th> </tr> </thead> <tbody> <tr> <td>Sep-18</td> <td>22</td> </tr> <tr> <td>Mar-19</td> <td>21</td> </tr> </tbody> </table> </div> <div data-bbox="1062 1267 1485 1682" style="flex: 1; padding-left: 20px;"> <p>WPD West Midlands reports on its payment performance every six months.</p> <p>Of invoices paid:</p> <ul style="list-style-type: none"> - 83% are within 30 days - 16% are within 31 to 60 days - 1% are in 60 days or more <p>This is based on the latest available data.</p> </div> </div>	Period	Average no. of payment days	Sep-18	22	Mar-19	21							
Period	Average no. of payment days													
Sep-18	22													
Mar-19	21													

Strategic report (continued)

For the year ended 31 March 2019

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 cost effectively accommodate these changes our network needs to become smarter and more flexible. Thus in 2017 WPD published its strategy for transition from the passive role of DNO to an active role as DSO using innovative solutions in order to mitigate the need for higher cost network reinforcement. 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 most from its existing electrical infrastructure by contracting services from distribution energy resources. In this way, costly network reinforcement and traditional redundancy-based model of energy systems can be avoided.

As a DSO, WPD West Midlands 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.

WPD is in process of implementing DSO strategy for all four DNOs and has taken a range of actions, including issuing a DSO Framework which assesses the technical issues associated with the transition. In addition WPD has 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. WPD will roll out its DSO strategy across its 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 WPD's existing innovation programme that develops and tests new solutions before deploying them as business as usual. WPD has developed significant competences in a number of key areas which will assist with transition to a DSO.

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

www.westernpower.co.uk/About-us/Our-Business/Our-network/Strategic-network-investment/DSO-Strategy.aspx

The priorities for DSO transition are also reflected within connections activities as detailed within the 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

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 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.

Strategic report (continued)

For the year ended 31 March 2019

Future developments (continued)

Low carbon networks/Network innovation competition (continued)

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

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 the 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 current year, WPD has set up the required customer engagement group ("CEG"), which will scrutinise our business plan for RIIO-ED2 and the process by which it is built. 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; stakeholder engagement process; and vulnerable customer strategies. Through its independent report to Ofgem, CEG will assist Ofgem and our stakeholders to understand whether our plans reflect and will meet the needs of our customers today and in the future.

The consultation for the RIIO-ED2 strategy will be launched in mid 2020, with Ofgem's decision expected to be published in early 2022 and late 2022 for fast track and slow track respectively.

WPD's RIIO-ED2 stakeholder engagement plan details are available at the link below:

<https://www.westernpower.co.uk/introduction-and-our-riio-ed2-engagement-plan>

Other political developments

As a result of the Labour Party's publication "Bringing energy home", the WPD Group has given serious consideration to the prospect of renationalisation of DNOs, should the Labour Party win a majority at the next UK general election. We do not believe that the proposed renationalisation of the DNOs is in the best interests of UK consumers. Specifically, Labour's proposal would be extremely costly for consumers while adding risk and unnecessary complexity at a time when significant additional investment is required to achieve the UK's low carbon targets.

Strategic report (continued)

For the year ended 31 March 2019

Future developments (continued)

Other political developments (continued)

The board believes that since privatisation in 1990, WPD has created significant value for customers and society in many ways. The WPD Group is investing £7.1 billion into the WPD network in the current RIIO-ED1 period and has already made significant investment to support the UK government in delivering a low carbon environment. WPD is leading the industry in the development of new ways of working and using innovative technologies. WPD has also led the industry for the last seven years in its level of customer service, with independent assessment demonstrating satisfaction levels over 90%, and we continue to look at ways to further improve this score.

Costs to customers are 17% lower than pre-privatisation on a like-for-like basis. WPD's costs account for around 17% of an average customer's yearly domestic electricity bill despite the huge increases in investment and tremendous improvements in both network reliability and customer service, with customers receiving a 60% improvement in reliability since then.

Risk management and controls

WPD West Midlands is exposed to various risks in the ordinary course of business that may have an adverse impact on the Company'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 WPD 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 WPD Group, is reported to the directors monthly.

WPD's processes and systems are continually evolving alongside the needs of the business and all WPD Group policies are reviewed by the business owners, on a maximum three year cycle, to ensure that they are relevant to the changing landscape of the business and industry practice.

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.

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

Strategic report (continued)

For the year ended 31 March 2019

Risk management and controls (continued)

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

	Risk	Mitigating actions
Safety	<p>On site accidents: Due to the nature of the business there is an inherent safety risk associated with unsafe working practices</p>	<ul style="list-style-type: none"> - WPD West Midlands has robust safety policies and procedures in place to ensure a safe working environment. There is a system for reporting of near misses and incidents and all the policies are reviewed and amended in response to any near misses or incidents that has occurred 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 2018 the Safety Team provided a package of presentations to support managers throughout WPD as part of the '2018 WPD Safety Week' programme. The package included an update for staff on the Company's health and safety statistics, a review of near miss and risk assessment procedures, planning emergency arrangements, vehicle condition checks, and site and office housekeeping. - 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 7,307 versus a target of 6,222.
Network performance & security	<p>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.</p>	<ul style="list-style-type: none"> - WPD West Midlands 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 West Midlands 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 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 West Midlands 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).

Strategic report (continued)

For the year ended 31 March 2019

Risk management and controls (continued)

	Risk	Mitigating actions
Network performance & security	<p>Cyber breach threat: Access to our key networks and systems by an unauthorised party.</p>	<ul style="list-style-type: none"> - 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.
Financial stability	<p>Interest rate risk: WPD West Midlands has had both short-term and long-term external debt during the year, at floating and fixed rates of interest, which exposes it to interest rate risk.</p>	<ul style="list-style-type: none"> - WPD West Midlands' interest rate risk management policy includes trying 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 the Company's regulated income, which is also index linked. - WPD West Midlands also uses forward-starting interest rate swaps to minimise exposure to cash flow interest rate risk for future forecast issuance of debt.
	<p>Credit rate risk: A customer or counterparty to a financial instrument will fail to perform and pay the amount due causing financial loss to the Company.</p>	<p>WPD West Midlands maintains credit policies and procedures with respect to counterparties. Depending on the creditworthiness of the counterparty, the Company may require collateral or other credit enhancements such as cash deposits or letters of credit and parent company guarantees.</p> <ul style="list-style-type: none"> - WPD West Midlands 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").

Strategic report (continued)

For the year ended 31 March 2019

Risk management and controls (continued)

	Risk	Mitigating actions
Financial stability	<p>Inflation risk: WPD West Midlands' index-linked borrowings and interest liabilities are exposed to a risk of change in the carrying value due to changes in the UK RPI.</p>	<p>WPD West Midlands' regulated assets ('RAV') 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.</p>
	<p>Impact of Brexit:</p>	<ul style="list-style-type: none"> - WPD West Midlands has evaluated the impact of Brexit on its operations, including review of all technical notices issued by the UK Government offering advice to businesses on a 'no deal' Brexit. - Potential inventory shortage due to restrictions between UK and EU borders has been identified as one of the key operational risks for WPD South West. In response to this risk, management has identified and ordered in bulk, critical stocks that merit stockpiling and has taken steps to secure additional supply for storage on site or at UK based suppliers. - Uncertainty around Brexit has resulted in the weakening of sterling; however the Company's revenues and assets are principally sterling denominated, thus minimizing any foreign currency risk for the Company. Any foreign currency debt is fully hedged by cross currency swaps.
Environment	<p>Regulatory changes: Changes in legislation relating to environmental and other matters are not adopted by WPD West Midlands.</p>	<ul style="list-style-type: none"> - WPD West Midlands has a dedicated regulation and compliance department with skilled personnel that track any regulatory changes and provide 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.

Strategic report (continued)

For the year ended 31 March 2019

Risk management and controls (continued)

	Risk	Mitigating actions
Environment	<p>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.</p>	<ul style="list-style-type: none"> - 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 West Midlands, 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 West Midlands 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: <ul style="list-style-type: none"> 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.
Stakeholder value & engagement	<p>Customer dissatisfaction: Failure to meet the required level of customer satisfaction performance.</p>	<ul style="list-style-type: none"> - WPD has a customer panel that meets four times a year and members, who represent a wide range of customers and other key stakeholder groups, help us keep up to speed with the issues affecting our customers. Through the panel, we proactively seek honest and challenging customer views about the way we operate and our future plans. It plays an important role in helping WPD develop its key priorities. The panel is attended by WPD's Chief Executive and other directors, demonstrating the commitment at every level to proactively engage with customers. - Ofgem requires us to design, establish and resource a new Customer Engagement Group ("CEG") as part of RIIO-ED2's enhanced engagement. The WPD Group was the first to set up a new CEG - a group of 15 members who will 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 understand the needs of its stakeholders so that they are aligned with the strategic priorities of the group. This year 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. A new online portal in place this year means even stakeholders who cannot attend can view content and videos and take part in the consultations.

Strategic report (continued)

For the year ended 31 March 2019

Risk management and controls (continued)

	Risk	Mitigating actions
Stakeholder value & engagement	<p>Lack of skilled employees: Failure to attract, retain and to develop our employees.</p>	<ul style="list-style-type: none"> - WPD maintains good 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 programs are offered under the Trainee Development Scheme and Technical Apprentice Scheme. - Succession plans are in place for key roles within the organisation.
	<p>Reliance on suppliers: WPD West Midlands relies on a limited number of suppliers for cable laying and tree cutting services, and for the supply of cables, plant and machinery.</p>	<ul style="list-style-type: none"> - 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 West Midlands' ability to operate the network. - Most of the electricity which enters WPD West Midlands' network is carried on the National Grid's grid supply points and thus the Company is dependent on National Grid. National Grid is regulated by Ofgem and thus the risk of a major failure is considered very remote.
	<p>Regulatory risk: WPD West Midlands' revenue is regulated and is subject to a review at the end of each price control period. Thus the Company 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.</p>	<ul style="list-style-type: none"> - 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.

Strategic report (continued)

For the year ended 31 March 2019

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.

In the year to March 2019, WPD Group assisted 306 separate charitable and non-charitable organisations as part of a £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 stakeholder and customer opinion research from our customer awareness activity. With regards to its customer groups WPD has launched the following activities:

- Vulnerable customers

WPD West Midlands 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.

Strategic report (continued)

For the year ended 31 March 2019

Corporate and social responsibility (continued)

Social and community (continued)

- Fuel poverty and energy affordability (continued)

In 2018/19, these projects supported over 16,000 fuel poor customers across WPD, leading to estimated annual savings of £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 West Midlands holds the Action on Hearing Loss (formerly RNID) 'Louder Than Words' charter mark accreditation, which assesses and endorses the accessibility of our services for deaf and hard of hearing people. We have held the accreditation for seven years. WPD is the first DNO Group 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 West Midlands 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 West Midlands is risk averse and thus does not engage in any aggressive or artificial tax planning to reduce its tax liabilities.

WPD West Midlands values an open working relationship with HM Revenue & Customs and keeps them 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 our tax strategy refer to the link below:

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

Human rights

WPD West Midlands is dedicated to conducting its business with honesty, integrity and fairness. In support of these principles, it is WPD West Midlands' 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 Company 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 West Midlands has robust policies on anti-corruption and anti-bribery. These policies apply to all employees of the WPD Group and form part of the employee Code of Conduct. Other individuals performing functions for the WPD 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.

Strategic report (continued)

For the year ended 31 March 2019

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 4 for details on our policy regarding the environment.

Refer to pages 9, 10 and 11 for details of impact of our activities on the environment and our performance in this area.

Refer to page 19 and 20 for our principal risks in relation to the environment and our actions to mitigate those risks.

- Employees

Refer to page 5 for details on our policies regarding employees.

Refer to pages 12 and 13 for our performance in relation to employee satisfaction.

Refer to page 21 for our principal risk in relation to employees and our actions to mitigate that risk.

- Social matters

Refer to pages 22 and 23 in relation to details on our policies and activities in relation to our social responsibilities.

- Human rights

Refer to page 23

- Anti corruption and anti bribery matters

Refer to page 23.

By Order of the Board



P Swift
Chief Executive Officer

18 July 2019

Western Power Distribution (West Midlands) plc

Avonbank

Feeder Road

Bristol BS2 0TB

For the year ended 31 March 2019

Director's report

For the year ended 31 March 2019

The directors present their annual report on the affairs of Western Power Distribution (West Midlands) plc, together with financial statements and auditor's report, for the year ending 31 March 2019.

Registered company number

The Company's registered number is 3600574.

Ownership

WPD West Midlands is an indirect, wholly-owned subsidiary of Western Power Distribution plc which is owned by PPL Corporation, an electricity utility of Allentown, Pennsylvania, US.

There were no transactions between WPD West Midlands and the ultimate owner.

Results, dividends and share capital

The profit for the year to 31 March 2019 is £196.7m (2018: £187.2m).

The Company also reports other comprehensive income, which was posted directly to capital and reserves, of £34.7m (2018: £0.3m). This primarily relates to the defined benefit pension plan remeasurement, net of tax.

For the year to 31 March 2019 dividends of £10.0m were paid by the Company (2018: £165.0m).

No share capital was issued by the Company in the year (2018: £50.0m).

Political donations and expenditure

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

Financial risk management objectives and policies

WPD does not undertake transactions in financial derivative instruments for speculative purposes. All debt at WPD West Midlands is denominated in sterling and therefore there is no currency risk exposure.

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

WPD West Midlands is supported by its credit facilities. At 31 March 2019, WPD West Midlands had committed borrowing facilities available, in respect of which all conditions precedent had been met at that date, of £300m maturing July 2021. At 31 March 2019, no borrowings had been drawn against the facility and no letters of credit issued.

On a day-to-day basis, WPD South West provides liquidity to the whole of WPD with balances with other group companies being settled periodically. It has borrowing arrangements in place with a range of third parties with high credit ratings. At 31 March 2019, WPD South West had committed borrowing facilities available in respect of which all conditions precedent had been met at that date of £245.0m maturing in July 2021, of which none was drawn. In addition, it had uncommitted facilities of £100.0m of which £5.0m can only be used for the issue of letters of credit; at 31 March 2019 no borrowings had been drawn and letters of credit of £3.5m were issued.

Director's report (continued)

For the year ended 31 March 2019

Financial risk management objectives and policies (continued)

Liquidity and going concern (continued)

At 31 March 2019, WPD West Midlands had £1,467.4m (2018: £1,434.9m) of external debt outstanding all of which was due after more than one year. It had cash and short-term deposits of £12.8m (2018: £6.9m).

The Company has net current liabilities of £77.6m (2018: £144.5m). The Company'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.

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

Dividend policy

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

Strategic report

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

- an indication of future developments in the business - see pages 14-16;
- an indication of activities of the Company in the field of research and development - see page 15;
- a statement on the policy for disabled employees - see page 5;
- employee policies - see page 5;
- greenhouse gas (carbon) emissions - see page 9.

Directors and their interests

The directors who served during the year and up to the date of signing the financial statements were, unless otherwise stated, as follows:

RA Symons, Chief Executive (deceased 7 November 2018)

P Swift, Chief Executive (appointed 7 November 2018)

IR Williams, Finance Director

AJ Sleightholm, Resources and External Affairs Director (appointed 1 April 2018)

G Halladay, Operations Director (appointed 14 January 2019)

ME Fletcher, non-executive independent director

AJ Cardew, non-executive independent director

Director's report (continued)

For the year ended 31 March 2019

Directors and their interests (continued)

During and at the end of the financial period, no director was interested in any contract of significance in relation to the Company's business other than service contracts. Insurance in respect of directors and officers is maintained by the WPD Group's ultimate parent, PPL Corporation. The insurance, which is third party qualifying indemnity insurance, is subject to the conditions set out in the Companies Acts and remains in force at the date of signing the Director's report.

Subsequent events

Subsequent to the year end, on 17 June 2019, the Company paid an interim dividend of £50.0m to WPD Distribution Network Holdings Limited.

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 re-appointment will be put before the Annual General Meeting.

By Order of the Board



P Swift
Chief Executive Officer

18 July 2019

Western Power Distribution (West Midlands) plc

Avonbank
Feeder Road
Bristol BS2 0TB

Directors' responsibilities statement

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom accounting standards and applicable law), 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 state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then 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 and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

Independent auditor's report to the members of Western Power Distribution (West Midlands) plc

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of Western Power Distribution (West Midlands) plc (the 'Company'):

- give a true and fair view of the state of the Company's affairs as at 31 March 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 "Reduced Disclosed Framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the profit and loss account;
- the statement of comprehensive income;
- the statement of changes in equity;
- the balance sheet;
- the statement of cash flows; and
- the related notes 1 to 26.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

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 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 (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. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Company.

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

Summary of our audit approach

Key audit matters

We identified the following key audit matter in the current year:

- Capitalisation of overheads.

Materiality

The materiality that we used in the current year was £11.8m (2018: £11.2m) which was determined on the basis of 5% of profit before tax.

Scoping

Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

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

Summary of our audit approach (continued)

Significant changes in our approach

Uncertain tax positions were presented as a key audit matter in the prior year but have not been included in the current year as we no longer consider this to meet the criteria. The remaining key audit matter consistent with the prior year.

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 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.

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.

- **Capitalisation of overheads**

Key audit matter description

Amounts capitalised as network assets include indirect costs associated with the engineering department and an element of 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 related to the capitalisation of engineering indirect costs and 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.

Given the magnitude of overheads capitalised in the business the impact could be material. Total engineering indirect costs and corporate overheads are £128.8m in the year (2018: £128.6m), of which £87.6m (2018: £89.1m) has been capitalised to fixed assets.

Refer to note 2 'Significant accounting policies' and note 3 'Critical accounting judgements and key sources of estimation uncertainty' in the financial statements for further discussion of the policy and judgements in relation to the capitalisation of overheads.

Independent auditor's report

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

Key audit matters - Capitalisation of overheads (continued)

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

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

- Evaluated the design and implementation of the key controls related to the classification of overheads as capitalisation expenditure and the appropriate percentage of costs to capitalise.
- Evaluated the appropriateness of the accounting treatment for capitalising overheads by reference to the requirements of IAS 16 Property, Plant and Equipment.
- We have tested an audit sample of costs capitalised. We have tested the percentage of costs capitalised through testing the inputs into management's assessment of the capitalisation rate and have tested the allocation of the individual cost categories capitalised on a line by line basis.

Key observations

Based on the work performed we conclude that the capital expenditure recorded is appropriate.

Our application of 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:

Materiality: £11.8m (2018: £11.2m)

Basis for determining materiality: 5% of the profit before tax. This is consistent with the previous year basis.

Rationale for the benchmark applied: Profit before tax is determined to be the key metric of the users of the financial statements

We agreed with the Board of Directors that we would report all audit differences in excess of £591,750, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to Board of Directors on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our audit was scoped by obtaining an understanding of the entity and its environment, including internal control, and assessing the risks of material misstatement. Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.

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.

Independent auditor's report

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

Other information (continued)

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.

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 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 company or to cease operations, or have no realistic alternative but to do so.

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 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.

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.

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, our procedures included the following:

- enquiring of management and internal audit, including obtaining and reviewing supporting documentation, concerning the Company's 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 related to fraud or non-compliance with laws and regulations.

Independent auditor's report

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

Extent to which the audit was considered capable of detecting irregularities, including fraud (continued)

Identifying and assessing potential risks related to irregularities (continued)

- discussing among the engagement team and involving relevant internal specialists, including tax, valuations, pensions, IT and industry specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud. As part of this discussion, we identified potential for fraud in the following areas: capitalisation of corporate overheads.
- obtaining an understanding of the legal and regulatory framework that the Company operates in, focusing on those laws and regulations that had a direct effect on the financial statements or that had a fundamental effect on the operations of the Company. The key laws and regulations we considered in this context included the relevant laws and regulations applicable to the group (including its components) and the sector it operates in such as UK Companies Act, Listing Rules, pensions legislation, tax legislation. In addition, compliance with terms of the Company's operating licence as set out by the energy regulator, Ofgem, were fundamental to the Company's ability to continue as a going concern.

Audit response to risks identified

As a result of performing the above, we identified capitalisation of overheads as a key audit matter. 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. As a result of performing the above, we did not identify any key audit matters related to the potential risk of fraud or non-compliance with laws and regulations.

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 relevant laws and regulations discussed above;
- enquiring of management, the audit committee and in-house/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 HMRC and OFGEM, the energy regulator;
- 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.

Report on other legal and regulatory requirements

Opinions on other matter 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 Director's report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic report and the Director's report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatement in the Strategic report or the Director's report.

Independent auditor's report

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

Other matters (continued)

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report in respect of the following matters 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, 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.

We have nothing to report in respect of these matters.

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.

Other matters

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 three years, covering years ending 31 March 2017 to 31 March 2019.

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

Our audit opinion is consistent with the additional report to those charged with governance we are required to provide in accordance with ISAs (UK).

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.

Delyth Jones

Delyth Jones, Senior Statutory Auditor
for and on behalf of Deloitte LLP
Statutory Auditor
Bristol, United Kingdom
19 July 2019

Profit and loss account

For the year ended 31 March 2019

	Note	2019 £m	2018 £m
Turnover	4	524.6	496.7
Operating expenses	5	(209.5)	(194.1)
Operating profit	6	315.1	302.6
Income from fixed asset investments		0.1	0.1
Profit on disposal of fixed assets		0.2	0.1
Profit before interest and tax		315.4	302.8
Interest receivable and similar income	7	0.3	0.1
Interest payable and similar charges	7	(78.4)	(77.7)
Net finance expense relating to pensions and other post retirement benefits	21	(0.6)	(0.6)
Profit before tax	4	236.7	224.6
Tax on profit	8	(40.0)	(37.4)
Profit for the financial year		196.7	187.2

All activities relate to continuing operations.

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

Statement of comprehensive income

For the year ended 31 March 2019

	Note	2019 £m	2018 £m
Profit for the financial year		196.7	187.2
Other comprehensive gain:			
<i>Other comprehensive loss to be reclassified to profit or loss in subsequent periods:</i>			
Reclassification adjustments for losses on cash flow hedges included in profit or loss (interest payable)		(0.8)	(0.8)
Income tax effect		0.1	0.2
		(0.7)	(0.6)
<i>Other comprehensive gain not to be reclassified to profit or loss in subsequent periods:</i>			
Re-measurement gains on defined benefit pension plan	21	42.9	1.1
Income tax effect		(7.5)	(0.2)
		35.4	0.9
Other comprehensive gain for the year, net of tax		34.7	0.3
Total comprehensive income for the year, net of tax, attributable to equity holder of the parent		231.4	187.5

Statement of changes in equity

For the year ended 31 March 2019

	Note	Share capital £m	Share premium account £m	Hedging reserve £m	Profit and loss account £m	Total equity £m
At 1 April 2017		185.1	713.6	3.1	344.5	1,246.3
Profit for the year		-	-	-	187.2	187.2
Other comprehensive (loss)/income		-	-	(0.6)	0.9	0.3
Total comprehensive (loss)/income for the year		-	-	(0.6)	188.1	187.5
Share issue		50.0	-	-	-	50.0
Equity dividends paid	9	-	-	-	(165.0)	(165.0)
At 31 March 2018		235.1	713.6	2.5	367.6	1,318.8
Change in accounting policy - IFRS 9		-	-	-	(0.1)	(0.1)
1 April 2018		235.1	713.6	2.5	367.5	1,318.7
Profit for the year		-	-	-	196.7	196.7
Other comprehensive (loss)/income		-	-	(0.7)	35.4	34.7
Total comprehensive (loss)/income for the year		-	-	(0.7)	232.1	231.4
Equity dividends paid	9	-	-	-	(10.0)	(10.0)
At 31 March 2019		235.1	713.6	1.8	589.6	1,540.1

Balance sheet

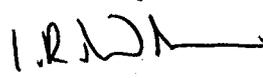
As at 31 March 2019

	Note	2019 £m	2018 £m
Non-current assets			
Tangible fixed assets	12	3,950.0	3,785.7
Intangible assets	13	7.6	4.3
Trade and other receivables	15	0.8	1.0
		3,958.4	3,791.0
Current assets			
Stocks	14	2.8	2.4
Trade and other receivables	15	110.0	114.3
Cash at bank and in hand	16	12.8	6.9
		125.6	123.6
Creditors			
Amounts falling due within one year	17	(203.2)	(268.1)
		(77.6)	(144.5)
Net current liabilities			
		3,880.8	3,646.5
Total assets less current liabilities			
Creditors			
Amounts falling due after more than one year	17	(2,151.9)	(2,086.8)
Provisions for liabilities			
Deferred tax	20	(205.2)	(181.5)
Other	19	(15.2)	(15.6)
Pension asset/(liability)			
	21	31.6	(43.8)
Net assets			
		1,540.1	1,318.8
Capital and reserves			
Called-up share capital	22	235.1	235.1
Share premium account	23	713.6	713.6
Hedging reserve	23	1.8	2.5
Profit and loss account	23	589.6	367.6
Equity shareholder's funds			
		1,540.1	1,318.8

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

The financial statements of the Company (registered number 3600574) on pages 35 to 73 were approved and authorised for issue by the Board of Directors on 18 July 2019 and were signed on its behalf by:


P Swift
Chief Executive


IR Williams
Finance Director

Statement of cash flows

For the year ended 31 March 2019

	Note	2019 £m	2018 £m
Operating activities			
Profit for the year		196.7	187.2
Adjustments to reconcile profit for the year to net cash flows from operating activities:			
Income tax expense		40.0	37.4
Interest payable		79.0	78.3
Interest receivable		(0.3)	(0.1)
Investment income		(0.1)	(0.1)
Depreciation of tangible fixed assets	6	68.7	66.7
Amortisation of customer contributions		(13.3)	(12.8)
Amortisation of intangible assets		0.8	0.5
Gain on disposal of tangible fixed assets		(0.2)	-
Difference between pension contributions paid and amounts recognised in the profit and loss account		(33.2)	18.6
(Decrease)/increase in provisions		(0.4)	1.5
Working capital adjustments:			
(Increase)/decrease in inventories		(0.4)	0.1
Decrease in trade and other receivables		6.5	0.3
(Decrease)/increase in trade and other payables		(4.2)	2.9
Interest paid		(77.4)	(76.8)
Interest received		0.3	0.1
Income taxes paid		(26.8)	(18.5)
Net cash from operating activities		235.7	285.3
Investing activities			
Purchase of tangible fixed assets		(232.6)	(277.1)
Purchase of intangible assets		(4.1)	(2.3)
Customers' contributions received		41.0	48.2
Proceeds from sale of tangible fixed assets		0.4	0.2
Transfers from Group		(0.5)	(0.1)
Dividends received		0.1	0.1
Net cash used in investing activities		(195.7)	(231.0)
Financing activities			
Net proceeds from issue of share capital		-	50.0
Net (decrease)/increase in short-term borrowings		(19.0)	19.0
Proceeds from long-term borrowings		30.8	-
Movement in balances with Group undertakings		(35.9)	37.1
Dividends or equivalent distributions paid		(10.0)	(165.0)
Net cash used in financing activities		(34.1)	(58.9)
Net increase/(decrease) in cash at bank and in hand		5.9	(4.6)
Cash at bank and in hand at beginning of year		6.9	11.5
Cash at bank and in hand at end of year	16	12.8	6.9

Notes to the financial statements

For the year ended 31 March 2019

1. Authorisation of financial statements and statement of compliance with FRS 101

The financial statements of Western Power Distribution (West Midlands) plc ("the Company") for the year ended 31 March 2019 were authorised for issue by the Board of Directors on 18 July 2019 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 shown on page 73.

The Company meets the definition of a qualifying entity under FRS 100 "Application of Financial Reporting Requirements".

2. Significant accounting policies

Basis of preparation

The financial statements have been prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework ("FRS 101") and in accordance with the provisions of the UK Companies Act 2006.

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, standards not yet effective, related party transactions and share based payments.

Where required, equivalent disclosures are given in the group accounts of Western Power Distribution plc. The group accounts of Western Power Distribution plc are available to the public and can be obtained as set out in note 26.

The financial statements have been prepared on the historical cost basis, except for 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 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 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 IAS 17, 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 a going concern basis as they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. This is discussed further under 'Financial risk management policies and objectives' within the Director's report.

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Impact of new International Financial Reporting Standards

Group financial statements

Group financial statements have not been prepared as the Company has taken advantage of the relief under s400 of the Companies Act 2006. The results of the Company are consolidated in the financial statements of Western Power Distribution plc. These financial statements therefore present information about the Company and not the Western Power Distribution (West Midlands) plc Group.

This note explains the impact of the adoption of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers on the Company's financial statements.

IFRS 9

IFRS 9 "Financial Instruments" supersedes IAS 39 "Financial Instruments: Recognition and Measurement". The adoption of IFRS 9 Financial Instruments from 1 April 2018, resulted in changes in accounting policies and adjustments to amounts recognised in the financial statements. In accordance with the transition provisions in IFRS, the Company has elected not to restate comparative figures on initial adoption of IFRS 9.

(i) Classification and measurement

On 1 April 2018, the Company's management assessed its financial instruments on the business model and cash flow characteristic test and reclassified its financial instruments into appropriate IFRS 9 categories. The main reclassifications are as below:

Financial Assets and Financial Liabilities - 1 April 2018	Loans and receivables £m	Amortised cost £m	Total £m
<i>Closing Balance 31 March 2018 - IAS 39</i>	119.0	-	119.0
Reclass Cash at Bank to Amortised Cost*	(6.9)	6.9	-
Reclass Trade and other receivables to Amortised Cost*	(112.1)	112.1	-
<i>Opening Balance 1 April 2019 - IFRS 9</i>	-	119.0	119.0

* These reclassifications have no impact on the measurement categories.

(ii) Impairment of Financial Instruments

Trade and other receivables

The Company applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all receivables including accrued income. This resulted in an increase of the loss allowance on 1 April 2018 by £0.1m. Debtors pertaining to revenue from providing distribution use of system services ("DUoS") are protected by Ofgem regulations and thus are subject to minimal credit risk, resulting in an immaterial impact of IFRS 9 on the Company ECL.

(iii) Total IFRS 9 impact

The total impact on the Company's retained earnings as at 1 April 2018 is as follows:

	2018 £m
Closing retained earnings 31 March 2018 - IAS 39	367.6
Increase in provision for trade and other receivables impairment	(0.1)
Opening retained earnings 1 April 2018 - IFRS 9	367.5

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Impact of new International Financial Reporting Standards (continued)

IFRS 15

IFRS 15 "Revenue from Contracts with Customers" effective for accounting periods beginning on or after 1 January 2018, supersedes the current revenue recognition guidance including IAS 18 Revenue and the related interpretations. IFRS 15 establishes a single comprehensive five-step model to account for revenues arising from contracts with customers, focusing on the identification and satisfaction of performance obligations.

The Company has assessed the impact of this standard and concluded that there will be 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 the profit and loss account.

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.

Turnover recognition

Distribution Use of System ("DUoS") Revenue

The Company, as a DNO, earns the majority of its turnover from providing distribution use of system services. The services are provided under a Distribution Connection and Use of System Agreements ("DCUSA") with its customers.

There is a single performance obligation under the DCUSA: the DNO is required to use its distribution network to deliver to its customers' electricity from metered entry points to exit point. WPD's performance obligations 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) *WPD's 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 performance obligation using the output method. Output method recognised revenue is based on direct measurements of value transferred to the customer. Accordingly WPD records turnover on a monthly basis, based on the amount of KWh of electricity delivered.

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

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Turnover recognition (continued)

Finance revenue

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

Customer contributions

Contributions receivable in respect of property, plant and equipment are treated as deferred income, which is credited to the profit and loss account over the estimated weighted life of the related assets of 69 years.

Other operating income and expense

Other operating income and expense includes 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.

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"); or as equity instruments designated at FVOCI, as appropriate. Financial assets include cash at bank and in hand, trade and other receivables. 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 the profit and loss account.

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 profit and loss account. 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.

Impairment of financial assets

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

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Impairment of financial assets (continued)

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. The Company 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.

The Company 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 ECL results 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.

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 ability of the customers' 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.

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 an original 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 group determines the classification of its financial liabilities at initial recognition. The measurement of financial liabilities depends on their classification, as follows:

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Financial liabilities (continued)

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 profit and loss account. 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.

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 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.

Finance costs

Finance expenses comprise interest payable on borrowings, the release of discount on provisions, and interest on pension scheme liabilities. Interest charges are recognised in the profit and loss account as they accrue, on an effective rate basis.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

WPD West Midlands as a lessee

Leases where the lessor retains a significant portion of the risks and benefits of ownership of the assets are classified as operating leases and rentals payable are charged to the profit and loss account on a straight-line basis over the lease term.

WPD West Midlands as a lessor

Assets leased out under operating leases are include in tangible fixed assets 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.

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation and impairments. Borrowing costs directly attributable to assets under construction and which meet the recognition criteria in International Accounting Standard ("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 capital schemes are capitalised within infrastructure assets together with the cost of materials and an appropriate proportion of overheads.

Contributions received towards the cost of tangible fixed assets 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 profit and loss account over the estimated economic useful lives of the assets to which they relate.

Depreciation is provided on all tangible fixed assets, 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
Fixtures and equipment	Up to 20
Vehicles and mobile plant	Up to 10

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable, 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 tangible fixed assets 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 profit and loss account in the period of derecognition.

Intangible assets

Intangible assets are stated at the amount initially recognised, less accumulated amortisation and accumulated impairment losses.

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Intangible assets (continued)

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.

Computer software

Costs directly associated with the development of computer software for internal use are capitalised where technical feasibility can be demonstrated, the Company is satisfied that future economic benefits will flow to the Company 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 tangible fixed assets and intangible assets

The Company assesses 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 Company 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.

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.

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.

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.

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Stocks

Stocks 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

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates and laws that are enacted or substantively enacted by the balance sheet date.

Deferred income tax is recognised on all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, with the following exceptions:

- 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;
- deferred income tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carried forward tax credits or tax losses can be utilised.

Deferred income tax assets and liabilities are measured on an undiscounted basis at the tax rates that are expected to apply when the related asset is realised or liability is settled, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date. Deferred income tax assets and liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities, the deferred income taxes relate to the same taxation authority and that authority permits the Company to make a single net payment.

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 the profit and loss account.

Pension benefits

The Company participates in one defined benefit pension plan, which is a section 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 Company also has an unfunded pension liability in respect of previous executives.

The ESPS is a group defined benefit pension plan that shares risks between entities under common control. Under FRS 101, the scheme has been accounted for as a defined benefit scheme by the Company as it has legal responsibility for the plan which it holds jointly with WPD East Midlands. The net defined benefit cost and net surplus or deficit of the plan have been allocated to WPD West Midlands and WPD East Midlands in accordance with pensionable salaries.

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

Pension benefits (continued)

The cost of providing benefits under the defined benefit plan is determined 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 amendments or curtailments occur. The current service cost (including administration costs) is allocated to the profit and loss account 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 profit and loss account.

Remeasurement 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.

Pension liability/asset recognised in the balance sheet represents the deficit or surplus in the 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 form of reduction in future contributions to the schemes.

Contributions to defined contribution schemes are recognised in the profit and loss account 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

Provisions are recognised when the Company has a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. 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.

Dividend distribution

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

Notes to the financial statements

For the year ended 31 March 2019

2. Significant accounting policies (continued)

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.

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.

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

Critical judgements in applying the Company's accounting policies

The following is the critical judgement, apart from those involving estimations (which are dealt with separately below), that the directors have made in the process of applying the Company'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. 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.

Uncertain tax positions

The Company's current tax charge and corporation tax liability reflects management's best estimate and judgement regarding the amount of tax payable for the current and previous tax returns that remain to be agreed with HM Revenue & Customs. 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 Company's tax position. In particular, the OECD Base Erosion and Profit Shifting ("BEPS") project has resulted in the Government recently 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 HM Revenue & Customs guidance and practical experience is still developing. Some of these rules may not directly apply to the Company, but apply to finance costs of PPL affiliate companies which may impact the amount of group loss relief available to the Company. Management has assessed the impact of this new legislation on the Company's tax position and has taken necessary actions to ensure that the Company is compliant with the rules.

Notes to the financial statements

For the year ended 31 March 2019

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

Uncertain tax positions (continued)

Management evaluates uncertain tax items which are subject to interpretation and agreement of the position with HM Revenue & Customs 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 HM Revenue & Customs, 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 HM Revenue & Customs may differ to that recorded in the financial statements, but management does not expect that any adjustments would have a material impact on the Company's financial results and positions.

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. The capitalisation rate is based on analysis of total labour cost, split between capital and expense. The rate is reviewed in detail annually and a reasonableness test is performed in light of total capital spend during the year. Information on sensitivity to the rate is as below:

	2019	2018
	Profit and loss account +/- £m	Profit and loss account +/- £m
Change in rate +/- 1%	0.4	0.3

Pension obligations

The Company has a commitment, mainly through the ESPS, to pay pension benefits. The cost of these benefits and the present value of the Company's pension liabilities depend on such factors as the life expectancy of the members, the salary progression of current employees and the discount rate at which the future pension payments are discounted. Based on advice from external actuaries, the Company 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. Refer to note 21 for sensitivity information.

4. Segmental reporting

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

Revenue from its five largest customers amounted to £102.6m, £63.7m, £63.2m, £58.6m and £58.5m (2018: £110.8m, £71.0m, £63.1m, £58.1m and £53.1m).

Other sources of revenue are not material and so are not shown separately.

Notes to the financial statements

For the year ended 31 March 2019

5. Operating expenses

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

	2019 £m	2018 £m
Employee costs (note 10)	42.9	40.2
Depreciation (note 6)	68.7	66.7
Amortisation of intangible assets (note 6)	0.8	0.5
Amortisation of customer contributions (note 6)	(13.3)	(12.8)
Property taxes	30.2	29.3
Other operating expenses	80.2	70.2
Operating expenses	209.5	194.1

6. Operating profit

	2019 £m	2018 £m
Operating profit is stated after charging/(crediting):		
Depreciation *	68.7	66.7
Amortisation of intangible assets	0.8	0.5
Operating lease rentals:		
Plant, machinery and equipment	2.5	2.8
Land and buildings	1.0	2.2
Amortisation of customer contributions	(13.3)	(12.8)
Research and development **	-	0.1
Auditor's remuneration:		
Fees payable to the Company's auditor for the audit of the Company's annual accounts	0.3	0.3
Non audit fee	-	-

* Depreciation of fixed assets is stated net of depreciation capitalised of £10.9m (2018: £9.6m) in respect of equipment consumed during the construction of the electricity network.

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

Notes to the financial statements

For the year ended 31 March 2019

7. Interest

	2019 £m	2018 £m
Interest receivable		
Interest on loans to other WPD undertakings	(0.3)	(0.1)
Interest payable		
Interest payable on bank loans and overdrafts	0.6	0.7
Interest payable on loans from other WPD undertakings	0.3	0.1
Interest payable on other loans	78.2	77.8
Less: interest capitalised	(0.7)	(0.9)
Total interest payable	78.4	77.7
Net interest expense	78.1	77.6

Interest in 2019 was capitalised at a rate of 2.4% (2018: 2.1%), based on the yield on the Company's borrowings.

8. Tax

Tax charged to the profit and loss account:

	2019 £m	2018 £m
Current tax:		
UK corporation tax on profits for the year (see below)	24.1	30.2
Adjustment in respect of prior years	(0.4)	(1.6)
Deferred tax (note 20):		
Origination and reversal of temporary differences	16.5	8.9
Impact of tax rate change	(0.4)	(0.2)
Adjustment in respect of prior years	0.2	0.1
Tax expense in the profit and loss account	40.0	37.4

Notes to the financial statements

For the year ended 31 March 2019

8. Tax (continued)

The tax on the Company's profit before tax differs from the theoretical amount that would arise using the standard rate of corporation tax in the UK of 19% (2018: 19%) as follows:

	2019	2018
	£m	£m
Profit before tax	236.7	224.6
Profit on before tax multiplied by standard rate of corporation tax in the UK of 19% (2018: 19%)	45.0	42.6
Effects of:		
Expenses not deductible and income not taxable for tax purposes	(0.1)	-
Group relief received at non-standard rates	(4.3)	(3.5)
Impact of tax rate change	(0.4)	(0.2)
Adjustments to tax charge in respect of prior years	(0.2)	(1.5)
Total tax expense reported in the profit and loss account	40.0	37.4

The total taxation expense as a percentage of profit before income tax gives an effective tax rate of 16.9% (2018: 16.7%) compared to the standard rate of 19% (2018: 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 to the Company ("group relief") by PPL affiliates not owned by the immediate parent undertaking are not paid for and therefore the Company benefits by the tax value of these losses. The impact of the tax rate change is due to the tax rate applicable to the future years when the majority of deferred taxation temporary differences are expected to reverse being lower than the tax rate applicable to the current year. Adjustments in respect of prior years mainly relate to the revised analysis of capital expenditure included in tax returns filed with HM Revenue & Customs and additional group relief received from PPL affiliates for no payment.

In addition to the amount charged to the profit and loss account, the following amounts relating to tax have been recognised in other comprehensive income.

	2019	2018
	£m	£m
Deferred tax:		
On cash flow hedges	(0.1)	(0.2)
On re-measurement of pension liabilities	7.5	0.2
Total tax charge in the statement of other comprehensive income	7.4	-

Notes to the financial statements

For the year ended 31 March 2019

8. Tax (continued)

UK corporation tax on profits for the year

The calculation of the amount of UK corporation tax payable on profits for the year is determined by tax legislation. The starting point for the calculation is the profit before tax shown in the profit and loss account 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 return for the year is filed with HM Revenue & Customs.

	2019	2018
	£m	£m
Profit on ordinary activities before tax multiplied by standard rate of corporation tax in the UK of 19% (2018: 19%)	45.0	42.6
Adjustments:		
Depreciation and amortisation (note i)	(7.5)	(7.6)
Pensions (note ii)	(8.8)	(1.0)
Other timing adjustments (note iii)	(0.1)	(0.1)
Other adjustments (note iv)	(0.2)	(0.2)
Corporation tax payable on profits before group relief	28.4	33.7
Group relief (note v):		
Losses received from other group companies payable at standard rate	(0.9)	(1.5)
Losses received from other group companies for free	(4.3)	(3.5)
Corporation tax payable on profits after group relief	23.2	28.7
The current tax charge on profits for the year is split as follows:		
Corporation tax payable to HM Revenue & Customs	23.2	28.7
Group relief payable to other group companies	0.9	1.5
	24.1	30.2

(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 profit and loss account. As a proportion of the pension expense is capitalised (see note 10), the deduction for contributions paid in a year is greater than the expense in the profit and loss account.

Notes to the financial statements

For the year ended 31 March 2019

8. Tax (continued)

UK corporation tax on profits for the year (continued)

(iii) Adjustments are required for the timing of other deductions. These include interest capitalised (see note 7) and employee benefit expense (see note 10). 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 profit and loss account 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

From 1 April 2017 the standard rate of corporation tax was reduced from 20% to 19%. In addition the Finance Act 2016 reduced the standard rate of corporation tax to 17% from 1 April 2020. This future change has been enacted and included in the calculation of deferred tax with respect to any temporary differences that are expected to reverse after the effective date.

9. Dividends

	2019	2018
	£m	£m
Dividends on equity shares:		
Interim dividends - 4.3 pence per share (2018: 70.2 pence per share)	10.0	165.0

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

Notes to the financial statements

For the year ended 31 March 2019

10. Employee benefit expense

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

	2019 £m	2018 £m
Wages and salaries	104.3	101.9
Social security costs	12.2	11.9
Pension costs	19.9	20.0
Total employee costs	136.4	133.8
Less allocated to capital expenditure	(93.5)	(93.6)
Charged to the profit and loss account	42.9	40.2

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 Company.

The average number of employees in the year was 2,016 (2018: 2,022). This includes a proportion of other WPD DNO staff who work in part for WPD West Midlands and excludes a proportion of WPD West Midlands staff who work in part for other WPD DNOs. All employees work for the network distribution business.

11. 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 paid director		Total	
	2019 £000	2018 £000	2019 £000	2018 £000
WPD Group				
The emoluments of the executive directors comprised:				
Base salary (note i)	465	607	1,520	1,629
Performance dependent bonus (note ii)	360	580	1,271	1,201
Pension compensation allowance (note iii)	212	-	363	345
Sub-total directors' remuneration	1,037	1,187	3,154	3,175
Long term incentive plan (note iv)	481	691	988	1,250
Fees to the independent non executive directors (note v, vi)	-	-	100	100
Other (note vii)	-	-	9,400	-
	1,518	1,878	13,642	4,525

Notes to the financial statements

For the year ended 31 March 2019

11. Directors' emoluments (continued)

- (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 21). 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; two executive directors exercised options (2018: none). In addition, the executive directors receive annually a grant of PPL Corporation shares which cannot generally be accessed for three years; a number of these shares is dependent on the achievement of certain criteria at PPL. The value of 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, five executive directors (2018: four) 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 has been booked in relation to death in service benefit.

Notes to the financial statements

For the year ended 31 March 2019

12. Tangible fixed assets

	Non network land & buildings £m	Distribution network £m	Fixtures & equipment £m	Vehicles & mobile plant £m	Total £m
Cost					
At 1 April 2018	13.7	4,907.5	70.1	30.6	5,021.9
Additions	-	230.0	12.1	1.5	243.6
Transfer from Group undertaking	0.5	-	-	-	0.5
Disposals and retirements	-	-	(4.1)	(0.4)	(4.5)
At 31 March 2019	14.2	5,137.5	78.1	31.7	5,261.5
Depreciation					
At 1 April 2018	0.2	1,192.9	29.9	13.2	1,236.2
Charge for the year	0.2	64.6	11.0	3.8	79.6
Disposals and retirements	-	-	(4.1)	(0.2)	(4.3)
At 31 March 2019	0.4	1,257.5	36.8	16.8	1,311.5
Net book value					
At 31 March 2019	13.8	3,880.0	41.3	14.9	3,950.0
At 31 March 2018	13.5	3,714.6	40.2	17.4	3,785.7

The net book value of land and buildings reported within distribution network assets comprises:

	2019 £m	2018 £m
Freehold	238.6	214.2
Short leasehold	6.2	6.3

Included within the Company's fixed assets are assets in the course of construction amounting at 31 March 2019 to £7.8m (2018: £29.2m) and land at a cost of £88.1m (2018: £82.5m).

Included in additions are staff costs of £93.5m (2018: £93.6m).

Notes to the financial statements

For the year ended 31 March 2019

13. Intangible assets

Computer
software
£m

Cost	
At 1 April 2018	5.1
Additions	4.1
At 31 March 2019	9.2

Amortisation	
At 1 April 2018	0.8
Charge for the year	0.8
At 31 March 2019	1.6

Carrying amount	
At 31 March 2019	7.6

At 31 March 2018	4.3
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14. Stocks

	2019	2018
	£m	£m
Raw materials and consumables	2.3	2.3
Work in progress	0.5	0.1
	2.8	2.4

The cost of stocks recognised as an expense during the year was £2.7m (2018: £2.6m).

Notes to the financial statements

For the year ended 31 March 2019

15. Trade and other receivables

	2019 £m	2018 £m
Current receivables		
Trade receivables	78.4	80.0
Amounts owed by other WPD undertakings	28.7	26.7
Accrued income	1.2	4.4
Prepayments	1.7	3.2
Total current receivables	110.0	114.3
Non-current receivables		
Other receivables	0.8	1.0
Total trade and other receivables	110.8	115.3

Amounts owed by other WPD undertakings are unsecured and are repayable on demand. Interest is received monthly at the Bank of England base rate at the end of the month.

16. Cash at bank and in hand

	2019 £m	2018 £m
Cash at bank	5.3	6.9
Short-term bank deposits	7.5	-
Cash at bank and in hand	12.8	6.9

Short-term deposits are measured at fair value through profit and loss (FVPTL).

At 31 March 2019, the Company had available £300.0m (2018: £300.0m) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met. All facilities incur commitment fees at market rates.

Included in cash and short-term bank deposits are restricted amounts totalling £5.0m (2018: £6.4m) which are not readily available for the general purposes of the Company. The restrictions relate to cash balances that can only be used for Low Carbon Network Fund projects.

For the purposes of the cash flow statement, cash at bank and in hand comprise the following at 31 March:

	2019 £m	2018 £m
Cash at bank and in hand (from above)	12.8	6.9

Notes to the financial statements

For the year ended 31 March 2019

17. Creditors

	2019 £m	2018 £m
Amounts falling due within one year:		
Short-term borrowing	-	19.0
Payments received on account	37.8	43.4
Trade creditors	9.9	11.3
Amounts owed to other WPD undertakings	7.5	41.4
UK corporation tax	10.5	13.6
Other taxation and social security	19.6	18.6
Other creditors	1.1	1.0
Deferred contributions	13.4	12.8
Accruals and deferred income	103.4	107.0
	203.2	268.1
	2019 £m	2018 £m
Amounts falling due after more than one year:		
Deferred contributions	684.4	651.9
Unsecured external borrowings repayable after more than five years:		
£250m 6.0% sterling bond 2025	248.3	248.0
£800m 5.75% bonds 2032	791.2	790.5
£400m 3.875% bonds 2024	396.9	396.4
£30m 0.01% indexed linked bonds 2028	31.1	-
	2,151.9	2,086.8

Amounts owed to other WPD undertakings are unsecured and are repayable on demand. Interest is paid monthly at the Bank of England base rate at the end of the month.

Unsecured borrowings are stated net of unamortised issue costs of £4.6m (2018: £5.0m) and discount on issue of £9.1m (2018: £10.1m). These costs, together with the interest expense, are allocated to the profit and loss account over the term of the bonds at a constant rate on the carrying amount.

All interest on bonds is paid annually.

Notes to the financial statements

For the year ended 31 March 2019

18. Net debt

	2019 £m	2018 £m
Short-term borrowings	-	19.0
Long-term borrowings	1,467.5	1,434.9
Amounts owed to other WPD undertakings	7.5	41.4
Less: Cash at bank and in hand	(7.8)	(0.5)
Net debt	1,467.2	1,494.8

Reconciliation of cash flows to net debt

Net (increase)/decrease in cash and cash equivalents	(7.3)	7.8
Net (decrease)/increase in short-term borrowings	(19.0)	19.0
Net (decrease)/increase in amounts owed to other WPD undertakings	(33.9)	31.6
Net increase in long-term borrowings	30.9	-
Change in debt resulting from cash flows	(29.3)	58.4
Net increase in borrowings due to indexation	0.5	-
Amortisation of premiums, discounts and issue costs	1.2	1.5
Movement in net debt in the year	(27.6)	59.9
Net debt at beginning of year	1,494.8	1,434.9
Net debt at end of year	1,467.2	1,494.8

19. Provisions for liabilities

	Deferred taxation (note 20) £m	Asset retirement obligations £m	Other £m	Total £m
At 1 April 2018	181.5	12.7	2.9	197.1
Arising/(released) during the year	23.7	0.6	(0.2)	24.1
Utilised during the year	-	(0.4)	(0.4)	(0.8)
At 31 March 2019	205.2	12.9	2.3	220.4

Asset retirement obligations ("ARO") relate to an estimate of the costs of dismantling and removing items of property, plant and equipment at the end of their useful life and are expected to be settled over the next 70 years.

The effect of discounting on AROs is not material and is therefore not shown separately.

Notes to the financial statements

For the year ended 31 March 2019

19. Provisions for liabilities (continued)

Other provisions at 31 March 2019 substantially relate to uninsured losses and an expected settlement of liabilities relating to the Electricity Association Technology Limited ("EATL") of £1.3m relating primarily to a pension deficit relating to that company. The liability in respect of the EATL is being settled over a period of approximately nine years; the directors expect the remaining provisions to be settled within the next two years.

20. Deferred tax

	Accelerated capital allowances £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 April 2017	181.0	(4.9)	(3.5)	172.6
Charge to the profit and loss account	10.5	(3.6)	1.9	8.8
Charge to equity	-	0.2	(0.1)	0.1
At 1 April 2018	191.5	(8.3)	(1.7)	181.5
Charge to the profit and loss account	10.1	6.2	-	16.3
Charge to equity	-	7.5	(0.1)	7.4
At 31 March 2019	201.6	5.4	(1.8)	205.2

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:

	2019 £m	2018 £m
Deferred tax liabilities	208.2	192.7
Deferred tax assets	(3.0)	(11.2)
Provision for deferred tax at 31 March	205.2	181.5

The net deferred tax liability due after more than one year is £206.1m (2018: £193.8m).

Deferred tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the deferred tax benefit through future taxable profits is probable. The Company did not recognise deferred tax assets of £40.3m (2018: £40.4m) in respect of capital losses amounting to £237.2m (2018: £237.5m) that can be carried forward against future taxable chargeable gains as there is no use of these assets for the foreseeable future.

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments

Electricity Supply Pension Scheme ("ESPS")

The ESPS provides pension and other related defined benefits based on final pensionable pay to employees throughout the electricity industry. One segment of the ESPS (the Central Networks Group segment) relates to WPD West Midlands and WPD East Midlands and most employees of these companies are members of the ESPS. These two companies are liable for the Central Networks Group segment and would benefit from any surplus if wound up. The assets are held in a trustee administered fund.

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

The asset or liability recognised in the balance sheet in respect of the defined benefit pension plan 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 credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows 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 scheme is a funded, defined benefit, final salary pension plan. The level of benefits provided depends on members' length of service and their salary at their date of leaving the Company. 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 scheme's investment strategy is decided by the Trustees, in consultation with the employer. The Board of Trustees must be composed of representatives of the employer and plan participants in accordance with the scheme's legal documentation.

The net defined benefit cost and net surplus or deficit of the plan have been allocated to WPD West Midlands and WPD East Midlands in accordance with pensionable salaries, currently 53.6% to WPD West Midlands (2018: 53.9%). The figures below show the proportion allocated to WPD West Midlands.

The Company also has an unfunded obligation which relates to previous executives.

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments (continued)

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

The amounts recognised in the WPD West Midlands' balance sheet are determined as follows:

	2019 £m	2018 £m
Present value of obligations	1,888.5	1,866.8
Fair value of scheme assets	(1,921.2)	(1,824.0)
(Surplus)/deficit of funded plan	(32.7)	42.8
Unfunded pension obligation (not part of ESPS)	1.1	1.0
Total pension (asset)/liability recognised in the balance sheet	(31.6)	43.8

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:

	2019 £m	2018 £m
Current service cost	17.1	17.5
Administrative costs	0.9	1.2
Past service costs and gains and losses on settlements*	3.7	-
Operating charge relating to defined benefit plans	21.7	18.7
Interest income on plan assets	(46.8)	(45.7)
Interest on plan liabilities	47.4	46.3
Other finance expense	0.6	0.6

The operating charge is allocated to the operating expenses in the profit and loss account or to capital expenditure as appropriate.

Analysis of the amount recognised in other comprehensive income:

	2019 £m	2018 £m
(Gain)/loss on plan assets excluding amounts included in interest income	(84.5)	9.4
(Gain)/loss from change in demographic assumptions	(70.3)	-
Loss/(gain) from change in financial assumptions	103.6	(22.2)
Experience losses	8.1	18.1
Change in percentage allocation rate	0.2	(6.4)
Remeasurement gain recognised in other comprehensive income	(42.9)	(1.1)

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments (continued)

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

The movement in the net defined benefit obligation over the accounting period is as follows:

	Year ended 31 March 2019			Year ended 31 March 2018		
	Present value of obligation £m	Fair value of plan assets £m	Total £m	Present value of obligation £m	Fair value of plan assets £m	Total £m
Liability/(asset) at 1 April	1,866.8	(1,824.0)	42.8	1,873.3	(1,848.7)	24.6
Current service cost	17.1	-	17.1	17.5	-	17.5
Administrative cost	0.9	-	0.9	1.2	-	1.2
Interest expense	47.4	(46.8)	0.6	46.3	(45.7)	0.6
Past service costs and gains and losses on settlements*	3.7	-	3.7	-	-	-
	69.1	(46.8)	22.3	65.0	(45.7)	19.3
Remeasurements:						
(Gain)/loss on plan assets excluding amounts included in interest income	-	(84.5)	(84.5)	-	9.4	9.4
(Gain) from change in demographic assumptions	(70.3)	-	(70.3)	-	-	-
Loss/(gain) from change in financial assumptions	103.6	-	103.6	(22.2)	-	(22.2)
Experience losses	8.1	-	8.1	18.1	-	18.1
Change in percentage allocation rate	(10.2)	10.4	0.2	6.9	(13.3)	(6.4)
	31.2	(74.1)	(42.9)	2.8	(3.9)	(1.1)
Contributions:						
Employer	-	(54.9)	(54.9)	-	-	-
Plan participants	2.9	(2.9)	-	2.9	(2.9)	-
	2.9	(57.8)	(54.9)	2.9	(2.9)	-
Payments from plan:						
Benefit payments	(80.6)	80.6	-	(76.0)	76.0	-
Administrative costs	(0.9)	0.9	-	(1.2)	1.2	-
	(81.5)	81.5	-	(77.2)	77.2	-
Liability/(asset) at 31 March	1,888.5	(1,921.2)	(32.7)	1,866.8	(1,824.0)	42.8

* Following the High Court ruling in October 2018, a Guaranteed Minimum Pension ("GMP") equalisation is required and various methods are permissible for the same. £3.7m represents the Company's estimate of likely additional pension liabilities using the default Method C2 for equalising for the effect of GMP.

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments (continued)

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

The significant actuarial assumptions made were as follows:

	2019	2018
RPI inflation	3.15%	3.00%
CPI inflation	2.05%	1.90%
Rate of general long-term salary increases	3.65%	3.75%
RPI linked pension increases (with 5% cap)	3.10%	2.95%
Post-88 GMP pension increases	1.90%	1.80%
Discount rate for scheme liabilities	2.36%	2.58%

Assumptions relating to future mortality are set based on actuarial advice in accordance with published statistics and experience. These assumptions translate into an average life expectancy in years for a member at age 60:

	31 March 2019	31 March 2018
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 2015 core projections and a 1.0% per annum long-term improvement rate
Life expectancy for a male currently aged 60	25.8	26.7
Life expectancy for a female currently aged 60	27.9	28.8
Life expectancy at 60 for a male currently aged 40	26.6	27.7
Life expectancy at 60 for a female currently aged 40	28.8	30.0

The sensitivity of the defined benefit obligation to changes in the principal assumptions is:

	Change in assumption %	Impact on defined benefit obligation £m
Discount rate	+/-0.50%	+172.9 / -152.2
RPI inflation	+/-0.50%	+152.9 / -137.4
Life expectancy	+ 1 year	84.3

The above sensitivity analysis on the discount rate is based on a change in that assumption while holding all other assumptions constant. The change in RPI inflation assumption impacts on the salary increases, 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 in the balance sheet.

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments (continued)

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

The Central Networks Group of the ESPS scheme assets are comprised as follows:

	31 March 2019		31 March 2018	
	Total £m	Of which not quoted in an active market £m	Total £m	Of which not quoted in an active market £m
Equities	355.2	-	328.0	-
Global credit	54.5	-	54.3	-
Property	67.4	67.4	110.5	110.5
Macro-orientated	205.6	205.6	192.0	192.0
Multi strategy	364.4	-	403.9	-
LDI strategy	818.4	-	741.0	-
Other	55.7	-	(5.7)	-
Total	1,921.2	273.0	1,824.0	302.5

There is no self-investment in the Scheme.

Through its defined benefit pension plan, the Company 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 scheme's long-term objectives.
Change in bond yields	A decrease in corporate bond yields will increase the scheme's liabilities, although this will be partially offset by an increase in the value of the scheme's bond holdings.
Inflation risk	The majority of the scheme's 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 that an increase in inflation will increase the deficit.
Life expectancy	The majority of the scheme's 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 Scheme uses government bonds, corporate bonds and cash as matching assets in the LDI Strategy holding. The remainder of the assets are used as growth assets.

The employer has agreed that it will aim to eliminate the scheme actuarial deficit (as assessed on the ongoing funding basis) by 31 March 2026.

Notes to the financial statements

For the year ended 31 March 2019

21. Pension commitments (continued)

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

The current agreed employer contributions are 27.9% per annum of pensionable salaries in respect of future benefit accrual, expenses (including PPF levies) and death in service benefits, plus an additional £2.0m per annum in respect of expenses. Company deficit contributions are £43.0m per annum payable from 1 April 2018 to 31 March 2021 and £25.8m per annum payable from 1 April 2021 to 31 March 2026.

Funding levels are monitored on a regular basis and the next triennial valuation is due to be completed as at 31 March 2019.

Current expected employer contributions to the WPD West Midlands segment of the scheme for the year ending 31 March 2020 are £56.5m. The results of the actuarial funding valuation as at 31 March 2019 may give rise to a revised schedule of contributions and as such the quantities above may be liable to change.

The weighted average duration of the defined benefit obligation is around 17 years.

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 and the following relates to the WPD Group as a whole:

- (a) a closed section with no active members. All of the active members in this scheme have transferred to the ESPS. At 31 March 2019 there were 199 members with deferred benefits in the scheme (2018: 204) and 5 pensioners (2018: 3). Market value of the assets was £2.1m (2018: £2.2m).
- (b) a new pension arrangement available to all new employees in WPD with effect from 1 April 2010. At 31 March 2019 there were 3,767 members (2018: 3,544). The market value of the assets of the open section of the scheme was £89.2m (2018: £73.9m). Employer contributions to the scheme across WPD amounted to £8.6m in the year (2018: £7.6m).

Notes to the financial statements

For the year ended 31 March 2019

22. Authorised and issued share capital

	2019 £	2018 £
Allotted, called-up and fully paid:		
235,050,000 ordinary shares of £1 each	235,050,000	235,050,000

23. Reserves

	Share premium account £m	Hedging reserve £m	Profit & loss account £m
At 1 April 2017	713.6	3.1	344.5
Profit for the financial year	-	-	187.2
Net movement on cash flow hedges (net of tax)	-	(0.6)	-
Dividends paid	-	-	(165.0)
Actuarial gains on defined benefit pension plan (net of tax)	-	-	0.9
At 31 March 2018	713.6	2.5	367.6
Change in accounting policy - IFRS 9	-	-	(0.1)
1 April 2018	713.6	2.5	367.5
Profit for the financial year	-	-	196.7
Net movement on cash flow hedges (net of tax)	-	(0.7)	-
Dividends paid	-	-	(10.0)
Actuarial gains on defined benefit pension plan (net of tax)	-	-	35.4
At 31 March 2019	713.6	1.8	589.6

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

The hedging reserve is stated net of tax and relates to:

- the effective portion of the cumulative net change in fair value of interest rate derivatives entered into in anticipation of the future issuance of long-term debt.
- the effective portion of the value paid in respect of interest rate derivatives associated with the issuance of existing long-term debt. The interest rate derivatives were settled in prior years and the gain continues to be amortised through the profit and loss account over the term of the debt.

Notes to the financial statements

For the year ended 31 March 2019

24. Contingent liabilities

Legal proceedings

WPD West Midlands is party to various legal claims, actions and complaints. Although WPD West Midlands 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 WPD West Midlands' financial statements.

25. Commitments

Capital commitments

Capital expenditure contracted for at the balance sheet date but not recognised in the financial statements is as follows:

	2019	2018
	£m	£m
Tangible fixed assets	7.2	10.3

Operating lease commitments - WPD West Midlands as lessee

WPD West Midlands leases various properties under non-cancellable operating lease arrangements. 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. WPD West Midlands also leases plant and machinery under non-cancellable operating leases which are usually very short-term.

Future minimum rentals payable under non-cancellable operating leases at 31 March are as follows:

	2019	2019	2018	2018
	Land &	Plant &	Land &	Plant &
	buildings	machinery	buildings	machinery
	£m	£m	£m	£m
In the first year	0.2	-	0.1	0.5
In the second to fifth year	0.8	0.1	0.2	1.9
In more than five years	0.4	0.1	0.1	0.6
	1.4	0.2	0.4	3.0

Notes to the financial statements

For the year ended 31 March 2019

26. Ultimate parent undertaking

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

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

The largest group in which the results of the Company are consolidated is that headed by PPL Corporation, 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.

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