

Western Power Distribution
RIIO Accounts for the Year Ended 31 March 2017

Contents	Page
Executive Summary & WPD Headlines for 2016/17	3
Introduction	4
RIIO Accounts	5
<hr/>	
<u>2016/17 Performance</u>	
Regulated Revenue	6-8
How WPD uses its Revenue	9
Total Expenditure (Totex)	10
Totex Incentive Mechanism (TIM)	11
Return on Regulated Equity (RoRE)	12-13
Operational Performance	14
Statement of Regulatory Financial Performance	15
Statement of Regulatory Financial Position	16
Statement of Regulatory Financial Performance (alternative view)	17
<hr/>	
Notes to Financial Statements	18-26
<hr/>	
<u>Appendices</u>	
Useful Links	27

Executive Summary

We present the RIIO accounts for Western Power Distribution (WPD), for the year ended 31 March 2017. This report contains information for the four Distribution Network Operators (DNOs) owned by WPD, and their combined total.

OFGEM plans to introduce a requirement for all network operators to produce RIIO accounts in the coming years. We are publishing our current proposal of the RIIO accounts for the first time on a voluntary basis.

WPD's RIIO accounts for 2016/17 have been prepared broadly in accordance with the form OFGEM proposed during discussions in 2017, although WPD's presentation is more concise.

We anticipate that the format and content of these RIIO accounts will be refined over future years and welcome any comments and feedback from stakeholders on our first proposal.

I confirm that this report and financial statements provide a fair representation of the regulatory position and returns of the WPD DNOs. The data in this report has been reviewed under WPD's Data Assurance process; the same framework is followed for WPD's regulatory submissions to OFGEM.



DCS Oosthuizen, WPD Finance Director

Date nd 2 March 2018

WPD Headlines for 2016/17

Cost to average customer per month	£8.50	See page 4
Network Availability	99.995%	See page 14
Total Expenditure (Totex)	£1,046m	See page 10
Network Asset Performance	157%	See page 14
Return on Regulatory Equity (RoRE)	6.5%	See page 12

Who we are

Western Power Distribution (WPD) is four of the fourteen Distribution Network Operators (DNOs) in the UK which deliver electricity to over 7.8 million homes and businesses.

WPD's network is the largest in the UK, operating from the Lincolnshire coast, across the Midlands, South Wales and the South West to the Isles of Scilly.

WPD are regulated by Ofgem who sets our revenues through a process known as a price control. The current price control is known as RIIO-ED1 and covers the period 2015-2023.



What we do

<p>We keep the lights on by operating our network assets effectively</p>	<p>We maintain equipment so that the network is in a condition to remain reliable</p>	<p>We fix the network if equipment gets damaged or is faulty</p>	<p>We connect customers by upgrading existing networks or building new ones</p>

Expenditure

WPD's Total Expenditure (Totex) in 2016/17 was **£1,046.3m**; WPD's Equity return for the same period was **£179.7m**.

Bill impact

WPD's costs account for around **16% of an average customer's yearly domestic electricity bill**, charged by suppliers.

This is approximately **£8.50 per month**.

Output highlights

Performance highlights for WPD for 2016/17 Regulatory Year include:

- Having the **highest customer satisfaction in the industry** for the sixth consecutive year.
- Being **number one for stakeholder engagement** for the sixth consecutive year.
- Providing **better than target network performance** for power cut duration and frequency.
- **Outperforming** Time to quote and Time to connect connections targets.
- **Reducing WPD's Business Carbon Footprint.**
- Proactively contacting **691,499 vulnerable customers** to confirm their details.
- **Supporting 11,766 fuel poor customers** to save over £3 million a year.

Purpose of this report

OFGEM intends to introduce a requirement for all electricity and gas network operators to produce RIO accounts in the coming years to replace the current Regulatory Accounts.

WPD is publishing RIO accounts for the first time on a voluntary basis and is keen to gather feedback from stakeholders on the format and content of this report.

Concept of RIO accounts

Network operators have a regulatory agreement with OFGEM. The intention of RIO accounts is that they reflect regulatory performance based on the outcome of this agreement, and recognise regulatory assets and liabilities on this basis. Differences from statutory reporting therefore include:

- Recognition of revenue or expenditure earlier or later than under Generally Accepted Accounting Principles.
- Recognition of defined benefit pension schemes on OFGEM's basis.
- Recognition of a single Regulatory Asset Value (RAV) rather than separate assets and liabilities of the regulated business.
- Enduring Value adjustments, which ensure any under or outperformance reported is for the whole price control, rather than as a short term timing difference.

Benefits of RIO accounts

- This set of accounts is intended to provide accurate and meaningful information to our stakeholders on WPD's financial position and financial performance under the regulatory framework.
- We hope this report provides clear and transparent reporting on WPD's financial and operational performance, including WPD's performance against incentives under the RIO price control arrangements.
- WPD is aiming to provide information which will enable readers to assess its stewardship of the DNOs' resources and the appropriateness of returns.

WPD has attempted to prepare these 2016/17 RIO Accounts in accordance with OFGEM's RIO Accounts principles using the latest available guidance, although WPD's presentation is more concise. Judgements have been made where OFGEM guidance is limited.

The values in this document are in **nominal prices** and in **£millions**, unless otherwise stated.

There may be minor differences in summary tables and charts between totals and the sum of components due to rounding.

The following abbreviations are used in this document:

WMID - Western Power Distribution (West Midlands) plc

EMID - Western Power Distribution (East Midlands) plc

SWALES - Western Power Distribution (South Wales) plc

SWEST - Western Power Distribution (South West) plc

Stakeholder feedback

WPD is keen to gain feedback from stakeholders on the format and content of RIO accounts.

Please provide all feedback to: riioaccounts@westernpower.co.uk

How our Regulated Revenue breaks down

WPD's Regulated Distribution Network Revenue (Regulated Revenue) comprises 3 elements

The largest element of the Regulated Revenue WPD receives is to cover the efficient costs of carrying out its regulated activities. This is **Base Demand Revenue** which was £1,410.3m in 2016/17, 90% of our Regulated Revenue.

Tariffs are set 15 months in advance based on forecast volumes and provided to energy suppliers for inclusion in customer bills, . Any actual amounts under or over recovered are adjusted through future years' revenues. This is called the **Under/(Over) recovery and K factor** which was £145.6m in 2016/17, 9% of our Regulated Revenue.

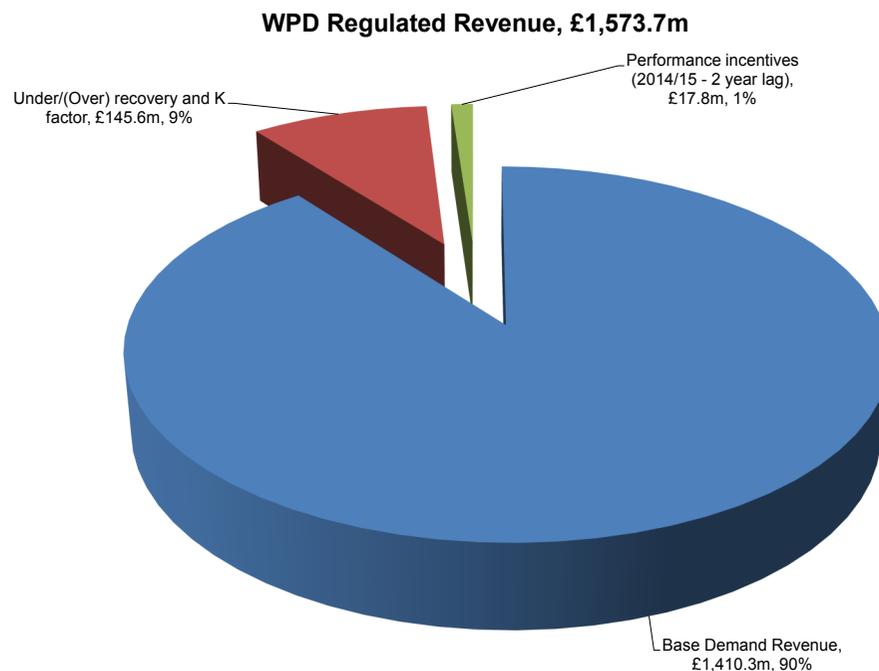
The third element relates to **Performance incentives**, i.e. penalties or rewards received under the various regulatory incentive schemes. This comprised £17.8m; 1% of Regulated Revenue in 2016/17.

The main incentives are:

- **Broad Measure of Customer Service (BMCS)**
Relating to customer satisfaction, complaints handling and stakeholder engagement
- **Connections incentives**
Relating to the time to quote and connect a customer
- **Interruptions Incentive Scheme (IIS)**
Relating to the number and durations of interruptions to electricity supplies.

WPD Regulated Revenue for the regulatory year to 31 March 2017 was £1,573.7m

Pages 7–9 provide a more detailed breakdown of this revenue.



How our Base Demand Revenue breaks down

Base Demand Revenue is the largest element of WPD's Regulated Revenue and is calculated in OFGEM's published Price Control Financial Model (PCFM).

Under the RIIO framework, WPD receives a Totex (Total Expenditure) allowance. 20% of this allowance is received in the year incurred; this is the **Fast pot expenditure allowance**. The remaining 80% is added to the Regulatory Asset Value (RAV) and funded over time through the **RAV depreciation allowance**.

Non controllable opex allowances relate to costs outside Totex which are recovered from OFGEM on a 'pass through' basis; these include licence fees, business rates and National Grid charges.

Allowance for return is calculated using the cost of capital and

comprises an allowance for the cost of debt and cost of equity.

Additional income is WPD's Fast Track reward. This equates to 2.5% of Totex over the price control.

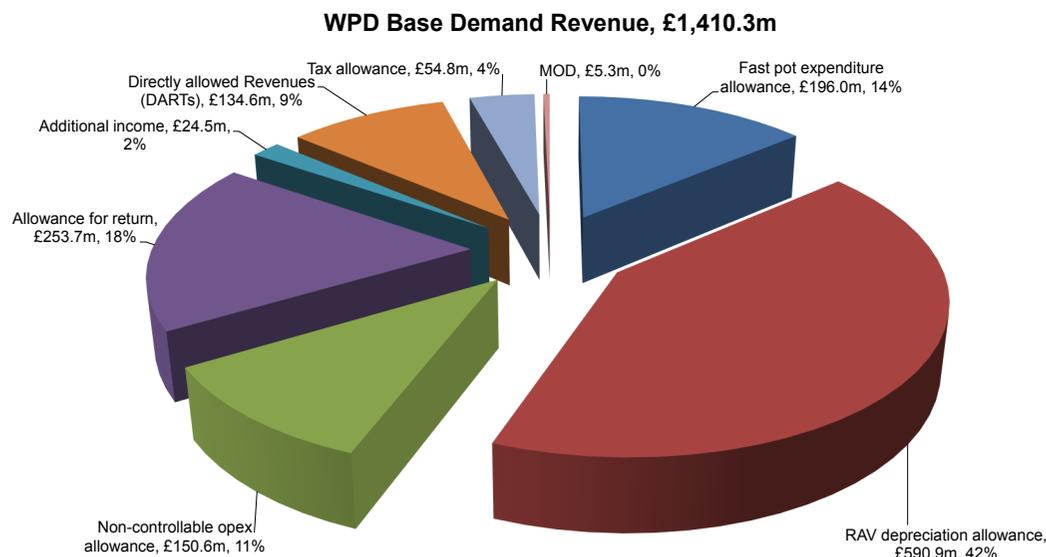
Direct Allowed Revenues (DARTs) includes allowances for pension deficit repair payments, revenue profiling adjustments and prior price control revenue to be recovered over RIIO ED1.

The **Tax Allowance** allows network operators to recover the tax charge, calculated by OFGEM's methodology.

MOD is an annual adjustment to Base Demand Revenue, calculated through OFGEM's Annual Iteration Process (AIP), to reflect updates to costs shared with customers and adjustments for uncertainty mechanisms.

WPD's 2016/17 Base Demand Revenue was £1,410.3m.

Base Demand Revenue + Under/over recovery
+ K factor + Incentive revenue
= Regulated Revenue



How our Performance Incentive Revenue breaks down

This element of WPD’s Regulated Revenue relates to performance incentives. These can result in penalties or rewards under each incentive scheme.

Incentive revenue received in the year includes the Broad Measure of Customer Service, Connections incentives and the Interruptions Incentive Scheme (IIS) .

Network Innovation Allowances (NIA) are funding mechanisms to improve network innovations via small scale projects.

Low Carbon Network Funds (LCNF) revenue adjustments relate to a prior price control (DPCR5) mechanism to encourage network operators to prepare for the role they will have to play as the UK moves to a low carbon economy.

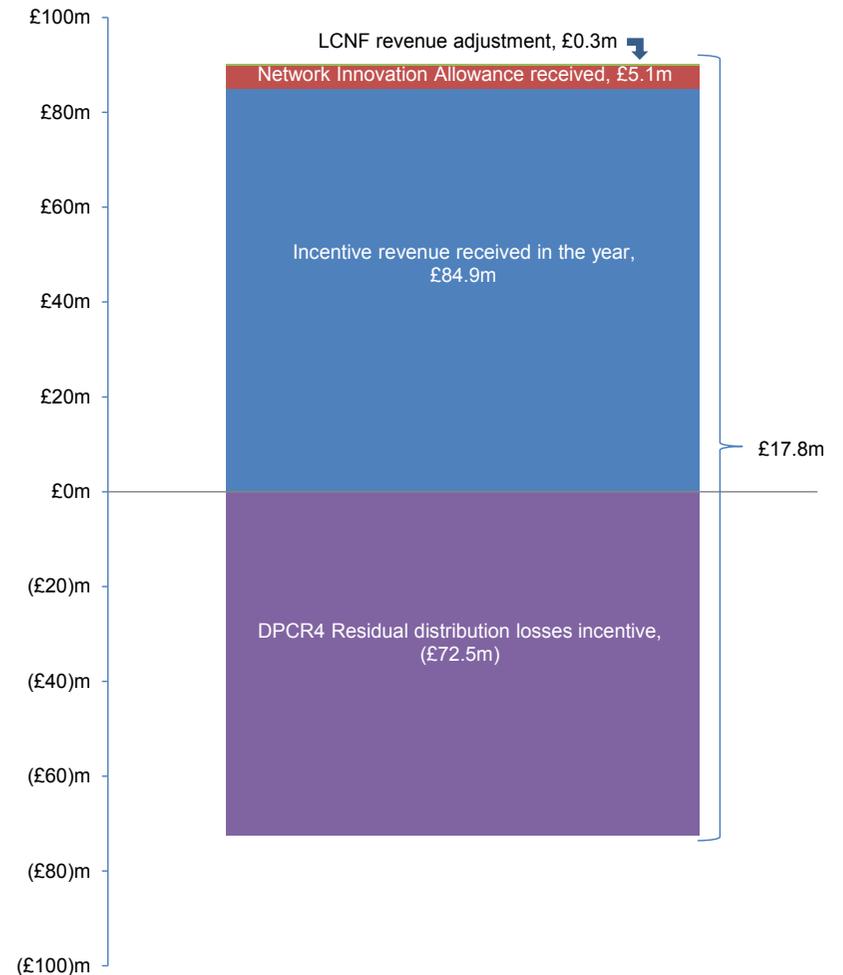
The **DPCR4 residual distribution losses incentive** relates to a prior price control (DPCR4) under which network operators were rewarded or penalised for residual losses on network assets.

Note that of the £17.8m Incentive Revenue, £12.7m relates to prior periods and is replaced in the RIIO accounts with incentive revenue earned in the year of £65.4m. The £12.7m comprises IIS, BMCS, Connections incentives, LCNF and DPCR4 residual losses amounts.

WPD 2016/17 Performance Incentive Revenue was £17.8m

Base Demand Revenue + Under/over recovery
+ K factor + **Incentive revenue**
= Regulated Revenue

WPD Incentive Revenue, £17.8m



How WPD uses its Revenue

This chart shows the regulatory view of how WPD uses its Regulated Revenue.

Investing and managing the network: Of the £1,573.7m Regulated Revenue received, £804.8m covers depreciation of the RAV and Fast Pot costs.

Financing costs: WPD's financing costs were £129.4m in 2016/17. This has been analysed as £126.9m of real interest costs and £2.5m other non-cash costs which are excluded from OFGEM's definition of interest.

Costs recovered for others: This covers 'pass-through' costs such as business rates, National Grid charges, smart meter costs and OFGEM licence fee.

Under/(Over) recovery, K factor: these amounts are timing differences on the recovery of revenues. K factor in 2016/17 includes £37.6m relating to the voluntary £5 per customer under-recovery in 2014/15.

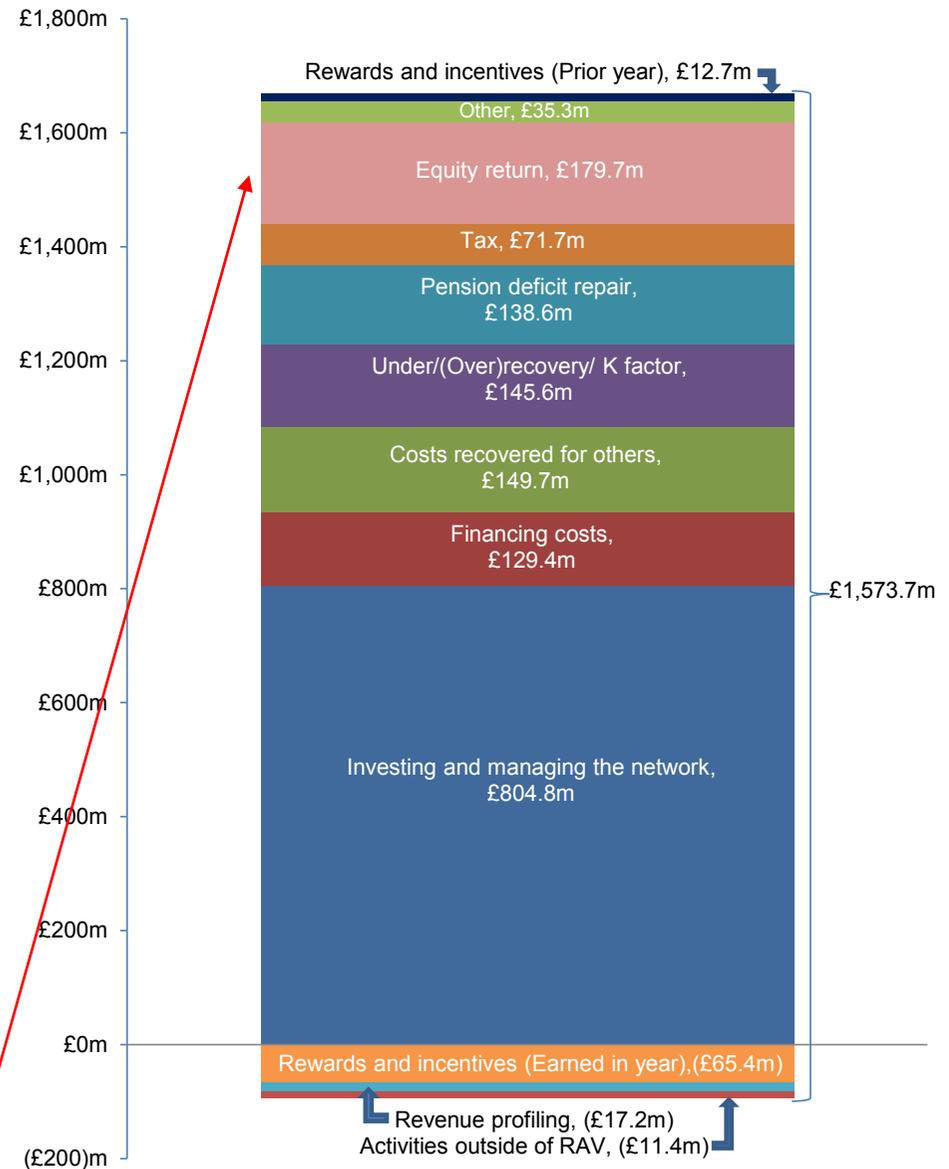
Pension deficit repair: £138.6m of WPD's revenue is to cover payments WPD makes to reduce the pension deficit related to historic regulated activity.

Tax: Of the £71.7m, £33.0m is WPD's current tax charge, plus a £61.0m movement in the tax asset recognised to reflect future tax allowances, offset by £22.2m deferred tax calculated in the RIIO accounts. This is different from the tax allowance WPD receives which only covers current tax and is calculated on a theoretical basis by OFGEM.

Rewards and Incentives: WPD's regulated revenue for 2016/17 includes incentive revenues of £12.7m which relate to previous years. In the RIIO accounts, this is replaced by incentive revenue earned in the year of £65.4m; £46.4m from the Interruptions Incentive Scheme, £22.7m from the Broad Measure of Customer Service and a £0.2m Losses Discretionary Reward, net of £3.4m borne by WPD under the Totex Incentive Mechanism, and £0.4m NIA and LCNF expenditure not covered by allowances.

Revenue Profiling adjustments in Base Revenue of £17.2m have been added in to reflect underlying revenue for the year.

Activities outside of RAV is the net amount earned from activities outside the price control which is added to Regulated Revenue.



Once all the costs above have been allocated, the remaining amount, i.e. revenues less costs, is the Equity return of £179.7m.

Total Expenditure (Totex)

10

How our costs are assessed

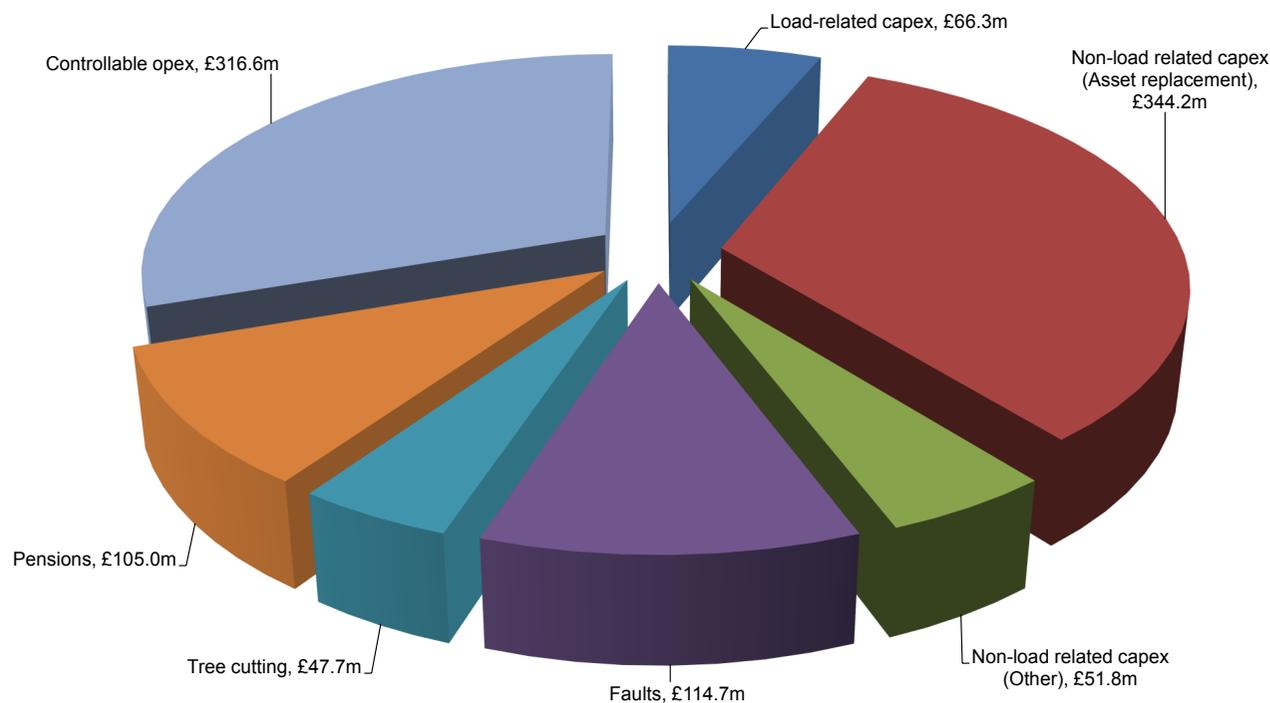
Under RIIO ED1, WPD's costs are assessed on a **Total Expenditure (Totex)** basis for its regulated business activities which includes both capital and operating expenditure.

Totex is a key feature in the business plan submission to OFGEM, as part of the price review process, as it underpins the Allowed Revenue set by OFGEM.

20% of this allowance is received in the year incurred; this is the **Fast pot expenditure allowance**. The remaining 80% is added to the Regulatory Asset Value (RAV) and funded over time through the **RAV depreciation allowance**.

The charts below represents WPD's 2016/17 actual costs broken down into the seven key reporting activities within Totex.

WPD Totex, £1,046.3m



WPD's 2016/17 Totex spend was £1,046.3m compared to an allowance of £978.5m.

This chart shows the breakdown of the total £1,046.3m spent.

Page 11 sets out how the overspend was funded between WPD and customers.

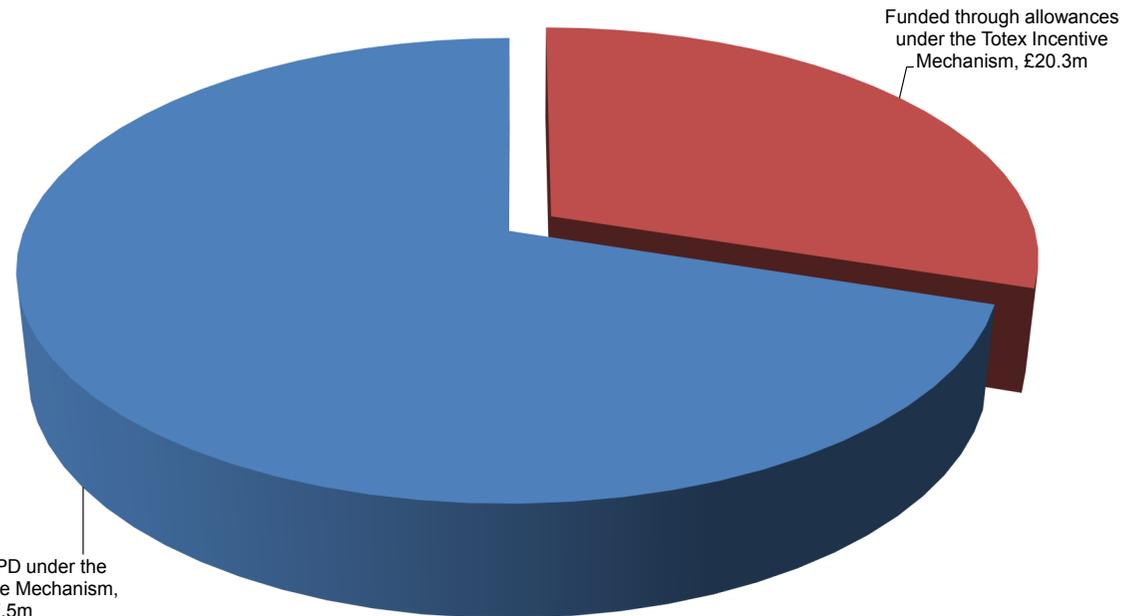
How our costs are assessed

As part of the RIIO ED1 price control, network operators are incentivised to spend efficiently through the Totex Incentive Mechanism (TIM). Any Totex under or overspend against allowances is shared between WPD and customers.

Under the TIM, WPD retains/(bears) 70% of any under/(over) spend on Totex, whilst the remaining 30% is returned/(funded) through adjusted allowances.

WPD Totex overspend was £67.8m for 2016/17. Of this, £47.5m (70%) will be borne by WPD and £20.3m (30%) will be funded through allowances. Adding the £20.3m additional amount funded to the original allowance of £978.5m gives the 'post-TIM Totex' WPD allowance of £998.8m.

WPD Totex Overspend, £67.8m



WPD's 2016/17 Totex overspend was £67.8m

70% (£47.5m) will be borne by WPD

30% (£20.3m) will be funded through allowances

A detailed Totex breakdown by WPD's 4 licence areas can be found on page 20

2016/17 Return on Regulatory Equity

How our performance is assessed

OFGEM assesses overall financial performance of network operators using a measure called Return on Regulatory Equity (RoRE). RoRE performance is compared to the cost of equity allowed at the start of the price control.

WPD was allowed a 6.4% cost of equity as part of its fast-track settlement.

Drivers of RoRE include performance under the TIM and performance against output incentives.

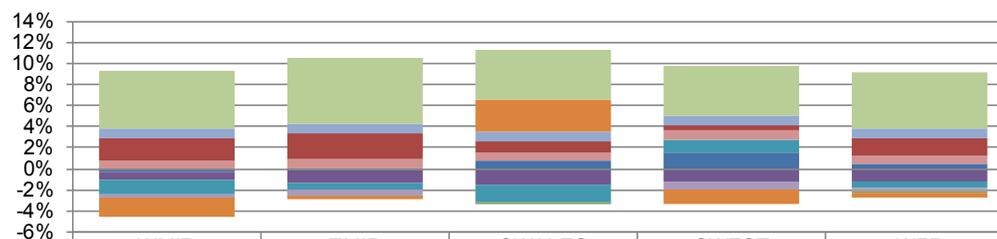
Totex underspends and incentive rewards increase network operators' returns, while overspends and incentive penalties decrease returns.

The Return on Regulatory Equity (RoRE) analysis below reflects 2016/17 performance using the RIIO accounts Statement of Regulatory Financial Performance and Statement of Regulatory Financial Position. It includes Financing and Tax variances, and Enduring Value adjustments.

Note that this view of RoRE uses **Regulatory Equity** calculated in the **Statement of Regulatory Financial Position**. The **Cost of Equity** allowance calculated on **35% of RAV** does not therefore equal 6.4% of Regulatory Equity calculated in this way.

This presentation of RoRE does not include under/over delivery of Network Asset Secondary Deliverables.

2016/17 RoRE - includes financing differences



Greater detail can be seen within note 7 on page 24

	WMID	EMID	SWALES	SWEST	WPD
Cost of Equity	5.5%	6.2%	4.6%	4.7%	5.4%
Totex Incentive Mechanism*	-1.9%	-0.3%	3.0%	-1.3%	-0.5%
IQI Additional Income	0.8%	1.0%	0.9%	0.9%	0.9%
Interruptions Related Quality of Service	2.2%	2.4%	1.1%	0.6%	1.7%
Broad Measure of Customer Service	0.8%	0.9%	0.7%	0.8%	0.8%
LCNF & Other Incentives	0.0%	0.0%	0.0%	0.0%	0.0%
Disallowed Related Party Margin & other	-0.2%	-0.6%	-0.1%	-0.8%	-0.4%
Financing	-1.3%	-0.6%	-1.6%	1.2%	-0.6%
Tax	-0.8%	-1.3%	-1.5%	-1.2%	-1.2%
Return on activities using assets outside the RAV	-0.3%	-0.1%	0.8%	1.6%	0.4%
RoRE Total	4.8%	7.7%	8.0%	6.4%	6.5%

* Totex Incentive Mechanism includes enduring value adjustment

ED1 Return on Regulatory Equity (as presented by OFGEM)

13

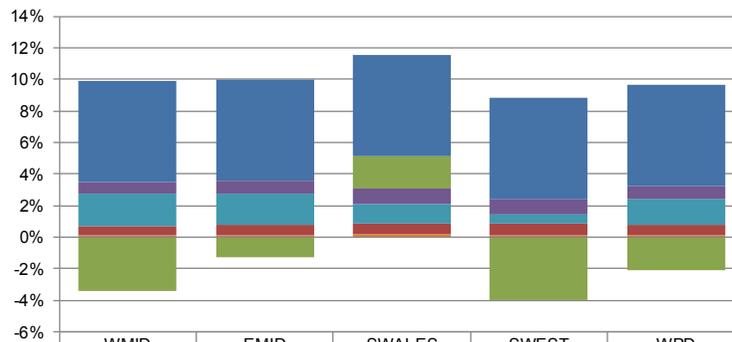
How our performance is assessed

The presentation of RoRE below aligns with **OFGEM's ED1 Annual Report**, with some small differences in assumptions. Note that this view of RoRE uses **35% of RAV as Regulatory Equity**.

This presentation of RoRE does not include Enduring Value adjustments, actual interest cost compared to the cost of debt allowance, tax variances, or under/over delivery of Network Asset Secondary Deliverables.

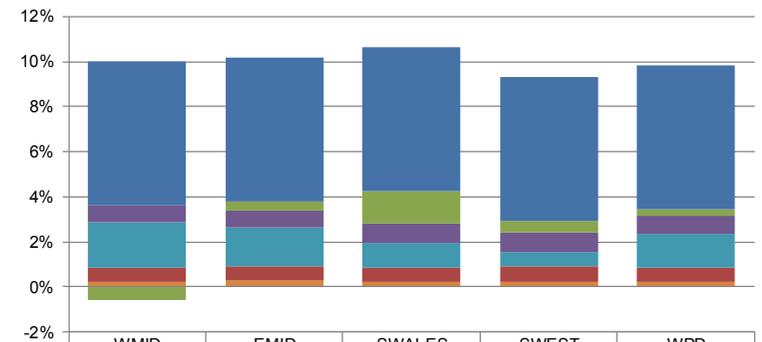
WPD's Return on Regulatory Equity (RoRE) over the eight year RIIO ED1 price control is forecast to improve compared to performance in the first two years of the price control. This will be achieved by bringing early Totex overspends broadly back in line with Totex allowances.

2016/17 RoRE



	WMID	EMID	SWALES	SWEST	WPD
Cost of Equity	6.4%	6.4%	6.4%	6.4%	6.4%
Totex Incentive Mechanism	-3.4%	-1.3%	2.1%	-4.0%	-2.1%
IQI Additional Income	0.7%	0.8%	1.0%	1.0%	0.8%
Interruptions Related Quality of Service	2.1%	2.0%	1.2%	0.6%	1.6%
Broad Measure of Customer Service	0.6%	0.6%	0.7%	0.7%	0.6%
Other	0.1%	0.2%	0.2%	0.2%	0.2%
RoRE Total	6.5%	8.7%	11.6%	4.9%	7.6%

8 Year forecast RoRE



	WMID	EMID	SWALES	SWEST	WPD
Cost of Equity	6.4%	6.4%	6.4%	6.4%	6.4%
Totex Incentive Mechanism	-0.6%	0.4%	1.4%	0.5%	0.3%
IQI Additional Income	0.7%	0.7%	0.9%	0.9%	0.8%
Interruptions Related Quality of Service	2.0%	1.7%	1.1%	0.6%	1.5%
Broad Measure of Customer Service	0.6%	0.6%	0.6%	0.6%	0.6%
Other	0.2%	0.3%	0.2%	0.2%	0.2%
RoRE Total	9.4%	10.2%	10.6%	9.3%	9.8%

Summary of incentivised performance

During RIIO-ED1 WPD committed to delivering 76 outputs for its customers. During 2016/17, the second year of the price control period, WPD has maintained high levels of service in all key areas.

The performance summary below demonstrates where outputs are directly related to financial outturn. These are outputs where a reward or penalty can be applied by the regulator as a result of over or under delivery.

A detailed review of operational performance over the year can be found in WPD's Business Plan Commitments Report 2016/17 which can be found at the link below:

www.westernpower.co.uk/About-us/Stakeholder-information/Performance-reporting-RIIO-ED1

Operational performance KPIs										
KPI	WMID		EMID		SWALES		SWEST		WPD TOTAL	
	Actual 16/17	Target								
Customer interruptions per 100 customers (excluding exceptions)*	56.1	85	43.2	51.1	38.0	49.9	48.3	55.4	47.6	62.6
Customer minutes lost (excluding exceptions)*	27.1	50.3	20.4	37.6	19.5	27.5	30.1	35.6	24.4	39.8
Network Availability	99.995%	99.990%	99.996%	99.993%	99.996%	99.995%	99.994%	99.993%	99.995%	99.992%
Guaranteed Standards of Performance failures **	4	0	0	0	0	0	11	0	15	0
Guaranteed Standards of Performance failures (Connections)	0	0	0	0	0	0	0	0	0	0
Guaranteed Standards of Performance failures (Number of 12 hour failure payments made)**	11	4064	1	2694	0	218	23	1623	35	8599
Overall Broad measure of customer satisfaction (Scores out of 10)	8.9	8.2	9.0	8.2	8.9	8.2	8.9	8.2	n/a	n/a
Stakeholder Engagement & Customer Vulnerability (Scores out of 10)	8.5	n/a	8.5	n/a	8.5	n/a	8.5	n/a	n/a	n/a
Connections time to connect incentive days:										
Time to quote LVSSA	4.52	8.21	3.48	8.21	4.30	8.21	5.16	8.21	n/a	n/a
Time to quote LVSSB	6.08	11.73	4.73	11.73	5.78	11.73	5.86	11.73	n/a	n/a
Time to connect LVSSA	37.18	42.08	34.40	42.08	33.76	42.08	36.53	42.08	n/a	n/a
Time to connect LVSSB	47.50	52.70	45.78	52.70	42.55	52.70	43.39	52.70	n/a	n/a
Connections incentive on customer engagement	No penalty	n/a								
Losses discretionary reward scheme £m	£0.04	N/A	£0.04	N/A	£0.04	N/A	£0.04	N/A	£0.16	n/a

Network asset indices performance					
	WMID	EMID	SWALES	SWEST	WPD
2015-16 percentage of target achieved	108%	171%	124%	105%	124%
2016-17 percentage of target achieved	160%	170%	152%	145%	157%
Percentage of RIIO-ED1 target achieved to date	34%	43%	35%	31%	35%

* Data is based on exceptional event information finalised by Ofgem in October 2017 and may therefore vary to other published data.

** WPD Internal target

KEY: Green = Better than target / Red = Worse than target

2016/17 Statement of Regulatory Financial Performance

15

Statement of Regulatory Financial Performance		WMID	EMID	SWALES	SWEST	WPD
	Notes	£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17
Regulated Distribution Network Revenue	1	495.9	481.8	239.9	356.1	1,573.7
Under/(over) recovery for the year		(1.8)	(6.7)	(1.5)	(12.2)	(22.2)
Allowed Revenue		494.1	475.1	238.4	343.9	1,551.5
K factor amount in allowed revenues		(29.5)	(61.3)	(11.4)	(21.2)	(123.4)
Underlying price control revenues for the year		464.6	413.8	227.0	322.7	1,428.1
LCNF successful delivery reward and IIS penalty protection award		0.0	0.0	2.5	0.0	2.5
Fast Money Spend	5	(64.0)	(63.1)	(30.1)	(52.1)	(209.3)
Regulatory depreciation		(190.4)	(186.7)	(93.2)	(125.2)	(595.6)
Pass through costs and adjustments to align revenues	2	(114.6)	(64.7)	(58.9)	(82.2)	(320.5)
Totex incentive value earned (Slow Pot only, net of Enduring Value)	3	(11.1)	(0.1)	12.5	(4.7)	(3.4)
Output incentives earned in the year	3	26.0	25.8	8.5	8.5	68.8
Revaluation movement in relation to incremental pension deficit and movement on unfunded pensions liability		0.2	(0.0)	(0.1)	(0.2)	(0.2)
Over/(under) recovery of other true-ups and provision movements		0.2	(0.8)	1.4	(1.7)	(0.9)
Disallowed Related Party margin, DRS 8 Income and removal of NBV of disposals		(2.5)	(3.7)	(1.7)	(3.6)	(11.5)
Under/(over) recovery for the year, interest		(0.1)	(0.1)	0.0	(0.2)	(0.3)
Time value for money in other regulatory balances		1.7	1.4	1.7	1.4	6.2
Return on activities using assets outside the RAV	10	(2.4)	(0.6)	3.8	10.6	11.4
Equity return before financing and tax		107.6	121.0	73.3	73.2	375.2
Income from Fixed Asset investments		0.0	0.0	0.0	5.6	5.6
Real net interest costs		(45.2)	(38.3)	(23.8)	(19.6)	(126.9)
Financing costs excluded from Ofgem interest definition, inc. amortisation of premia and issue costs, and derivative mover		(1.4)	(0.7)	0.1	(0.5)	(2.5)
Current Tax Charge		(12.4)	(11.1)	(4.0)	(5.5)	(33.0)
Movement in future taxation recovery		(20.9)	(18.3)	(6.9)	(14.8)	(61.0)
Deferred Tax Movement		14.1	6.5	(2.3)	3.9	22.2
Equity return for the year		41.8	59.1	36.4	42.2	179.7

2016/17 Statement of Regulatory Financial Position

16

Statement of Regulatory Financial Position		WMID		EMID		SWALES		SWEST		WPD	
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
	Notes	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17
Fixed assets & equivalents											
Regulatory Asset Value	8		2,261.4		2,255.9		993.5		1,465.4		6,976.2
Other regulatory balances	9		165.1		123.3		115.0		123.9		527.3
Fixed assets outside RAV (Non regulatory fixed assets)		181.6		242.6		130.9		185.7		740.6	
Deferred contributions (Relating to activity outside RAV)		(179.1)		(251.3)		(126.7)		(181.2)		(738.4)	
Fixed assets outside RAV (Net of deferred contributions)	10		2.4		(8.8)		4.1		4.4		2.2
Investments			0.0		0.0		0.0		42.4		42.4
			<u>2,428.9</u>		<u>2,370.4</u>		<u>1,112.6</u>		<u>1,636.1</u>		<u>7,548.1</u>
Current Assets:											
Inventory			2.5		10.8		1.3		8.0		22.6
Trade and other receivables			121.1		96.7		61.1		83.5		362.4
Corporation tax			0.0		0.0		4.6		2.9		7.5
Unamortised debt issuance costs, discount/premia on issue (excluded from OFGEM net debt definition)			16.6		(48.4)		5.0		4.6		(22.2)
Cash and cash equivalents	6		11.5		11.3		19.5		21.6		63.9
			<u>151.7</u>		<u>70.4</u>		<u>91.5</u>		<u>120.6</u>		<u>434.2</u>
Creditors - Amounts falling due within one year											
Short term borrowings, bank loans and overdrafts	6		0.0		(125.0)		0.0		(105.4)		(230.4)
Trade and other payables			(187.8)		(156.6)		(75.6)		(175.7)		(595.7)
Corporation tax			(3.6)		(1.3)		0.0		0.0		(4.9)
			<u>(191.4)</u>		<u>(282.9)</u>		<u>(75.6)</u>		<u>(281.1)</u>		<u>(831.0)</u>
Creditors - Amounts falling due after more than one year											
Borrowings	6		(1,452.5)		(1,332.2)		(624.8)		(757.5)		(4,167.0)
			<u>(1,452.5)</u>		<u>(1,332.2)</u>		<u>(624.8)</u>		<u>(757.5)</u>		<u>(4,167.0)</u>
Provisions for liabilities and charges											
Deferred taxation		(107.1)		(88.2)		(70.2)		(81.7)		(347.1)	
Amounts recoverable or payable in respect of future taxation		97.8		91.3		52.7		72.2		314.0	
Deferred taxation (net)			(9.3)		3.2		(17.5)		(9.5)		(33.1)
Other provisions for liabilities and charges			(14.1)		(12.6)		(84.7)		(13.2)		(124.6)
			<u>(23.4)</u>		<u>(9.4)</u>		<u>(102.2)</u>		<u>(22.7)</u>		<u>(157.7)</u>
Pension liability											
Post employment benefits		(211.4)		(216.8)		(36.7)		(188.1)		(653.0)	
Pension liability funding recoverable		169.6		171.8		91.3		148.6		581.3	
Post employment benefits (net)			<u>(41.8)</u>		<u>(45.0)</u>		<u>54.6</u>		<u>(39.5)</u>		<u>(71.7)</u>
Net assets			<u>871.5</u>		<u>771.3</u>		<u>456.1</u>		<u>655.9</u>		<u>2,754.8</u>
Capital and reserves											
Issued share capital and reserves attributable to owners or parent											
Called-up share capital			185.1		207.6		291.7		438.2		1,122.6
Share premium account			713.6		46.2		23.2		4.1		787.1
Reserves			(27.2)		517.5		141.2		213.6		845.1
Equity shareholders' funds			<u>871.5</u>		<u>771.3</u>		<u>456.1</u>		<u>655.9</u>		<u>2,754.8</u>

2016/17 Statement of Regulatory Financial Performance

17

Statement of Regulatory Financial Performance (Alternative view)		WMID		EMID		SWALES		SWEST		WPD	
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
	Notes	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17	2016/17
Allowances for the cost of capital on the RAV		81.7		81.2		35.6		52.2		250.8	
less: cost of debt allowances		(33.4)		(33.2)		(14.6)		(21.3)		(102.4)	
Equity return on Regulated Asset Value		48.3		48.0		21.1		30.9		148.3	
Gain/(Loss) under Totex incentives	5	(25.8)		(9.7)		7.2		(19.2)		(47.5)	
Enduring value adjustment	3, 9	9.5		7.7		6.7		10.6		34.6	
Additional income/IQI		7.1		7.5		4.0		5.8		24.4	
Gain/(Loss) under output incentives	3	26.0		25.8		8.5		8.5		68.8	
Disallowed Related Party margin, DRS 8 Income and removal of NBV of disposals		(2.5)		(3.7)		(1.7)		(3.6)		(11.5)	
Revaluation movement in relation to incremental pension deficit and movement on unfunded pensions liability		0.2		(0.0)		(0.1)		(0.2)		(0.2)	
Over/(under) recovery of other true-ups		0.3		(2.5)		1.4		3.9		3.0	
Provision liability movement		(0.1)		1.8		0.0		(5.6)		(3.9)	
Other		0.2		(0.2)		(0.1)		0.4		0.4	
Equity return on RAV before financing variances		63.3		74.6		46.9		31.6		216.4	
Income from Fixed Asset investments		0.0		0.0		0.0		5.6		5.6	
Variances to allowance - Real cost of debt - Interest		(10.9)		(7.4)		(10.1)		(3.9)		(32.3)	
Variances to allowance - Real cost of debt - Other costs		(0.9)		2.3		0.8		5.7		7.8	
Financing costs excluded from Ofgem interest definition, inc. amortisation of premia and issue costs, and derivative mover		(1.4)		(0.7)		0.1		(0.5)		(2.5)	
Interest in K-factor		(0.1)		(0.1)		0.0		(0.2)		(0.3)	
Time value for money in other regulatory balances		1.7		1.4		1.7		1.4		6.2	
Equity return on RAV before tax and gearing variances		51.6		70.1		39.5		39.6		200.8	
Variances to allowance - Tax		(6.9)		(10.1)		(6.7)		(6.8)		(30.5)	
Tax variance relating to gearing variance		(0.5)		(0.3)		(0.1)		(1.1)		(2.0)	
Total Equity return on the RAV		44.2		59.7		32.7		31.6		168.3	
Return on activities using assets outside RAV	10	(2.4)		(0.6)		3.8		10.6		11.4	
Total Equity return for the year		41.8		59.1		36.4		42.2		179.7	

2016/17 Notes to Financial Statements

18

1. Analysis of Revenue - Components of total earned Regulatory Revenue		WMID	EMID	SWALES	SWEST	WPD
	Comments	£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17
Fast pot expenditure allowance	(i)	56.7	60.6	32.0	46.8	196.0
Non-controllable opex allowance	(ii)	45.0	51.4	27.0	27.2	150.6
RAV depreciation allowance	(iii)	189.1	182.8	93.1	125.9	590.9
Allowance for return	(iv)	82.7	80.5	36.5	54.0	253.7
Additional income	(v)	7.1	7.6	4.0	5.8	24.5
Direct Allowed Revenues (DARTs)	(vi)	33.4	34.2	21.2	45.7	134.6
Tax allowance	(vii)	18.8	16.6	7.6	11.8	54.8
Allowed Base Revenue	(viii)	432.7	433.6	221.3	317.3	1,404.9
Modification to Base Revenue from Annual Iteration Process (MOD)	(ix)	0.9	6.4	(0.1)	(1.8)	5.3
Base Demand Revenue	(x)	433.6	440.0	221.2	315.4	1,410.3
Incentive revenue received in the year	(xi)	38.8	31.8	6.4	8.0	84.9
Network Innovation Allowance received	(xii)	1.6	1.6	0.8	1.1	5.1
LCNF Revenue adjustment	(xiii)	0.1	0.1	0.0	0.1	0.3
DPCR4 Residual distribution losses incentive	(xiv)	(9.5)	(59.7)	(1.4)	(1.9)	(72.5)
Correction ("K) factor	(xv)	29.5	61.3	11.4	21.2	123.4
Under/Over recovery	(xvi)	1.8	6.7	1.5	12.2	22.2
Regulated Distribution Network Revenue	(xvii)	495.9	481.8	239.9	356.1	1,573.7

This shows 2016/17 revenue for our regulated business, for activities within the RIIO ED1 price control.

Final determination Base Revenue Allowances are calculated in OFGEM's externally published Price Control Financial Model (PCFM).

OFGEM sets the amount of revenue each DNO is allowed to charge customers each year over the 8 year price control. This is adjusted dependent on DNOs' operational and financial performance each year in order to drive efficiencies and performance for customers.

Comments:

- (i) An allowance based on 20% of Totex that can be recovered in the year of expenditure.
- (ii) An allowance for 'Pass through' items/costs, not included within Totex, i.e. licence fees, business rates and exit charges.
- (iii) Depreciation allowance calculated on a licensee's RAV balance.
- (iv) An allowance based on a vanilla Weighted Average Cost of Capital (WACC) applied to the RAV.
- (v) This is WPD's 'Fast Track' reward for business plans deemed to be of particularly high quality, efficient and value for money. This award equated to 2.5% of Totex over the life of the price control.
- (vi) This includes allowance for pension deficit repair payments and prior price control revenue to be recovered in ED1.
- (vii) An allowance to take account of existing and announced corporation tax rates, writing down allowance rates, existing legislation, accounting standards, HM Revenue & Customs (HMRC) policy and modelled levels of gearing and corporate debt interest payments for the licensee.
- (viii) The core amount of money that a network company can earn on its regulated business in order to recover the efficient costs of carrying out its activities.
- (ix) An annual adjustment, calculated within an Annual Iteration Process (AIP), to Base Revenue in light of updates to actual Totex and adjustments for other uncertainty mechanisms. These are calculated within the Annual Iteration Process.
- (x) The amount included in the licensee's Allowed Distribution Network Revenue for a particular Regulatory Year, that is derived in accordance with the formula set out in paragraph 2A.5 of CRC 2A of the licence.
- (xi) A reward mechanism designed to drive continuous improvement in operational performance. These include Broad Measure, Incentives on connections and Customer Interruption performance.
- (xii) A reward mechanism based on a set, use-it-or-lose-it allowance for each DNO to fund small-scale innovative projects.
- (xiii) A DPCR5 reward mechanism designed to encourage the DNOs to prepare for the role they will have to play as the UK moves to a low carbon economy.
- (xiv) A reward/penalty mechanism relating to a prior price control (DPCR4) incentive scheme to reduce residual losses from DNO assets.
- (xv) The corrective 'k' factor is applied by the regulator, on a 2 year lag, to account/recover for under or over recovery of previous years' revenues.
- (xvi) An under/over recovery adjustment to return a DNO's financial performance to reflect actual Allowed Revenue charged to Distribution Use of System (DUoS) customers in the current financial year.
- (xvii) The total amount of Regulated Distribution Network Revenue charged to DUoS customers in the current financial year.

2016/17 Notes to Financial Statements

19

2. Pass through costs and adjustments to align revenues

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
Adjustment to remove IIS revenue from previous years included in 2016/17 Regulated Revenue	(36.0)	(28.3)	(4.7)	(5.8)	(74.8)
Adjustment to remove Broad Measure & Time To Connect revenue from previous years included in 2016/17	(2.8)	(3.5)	(1.7)	(2.2)	(10.1)
Adjustment to remove LCNF successful delivery and IIS protection reward from previous years included in 2016/17	0.0	0.0	(2.5)	0.0	(2.5)
Adjustment to add back DPCR4 distribution losses penalty included in 2016/17 Regulated Revenue	9.5	59.7	1.4	1.9	72.5
Add back Revenue Profiling adjustments to Regulated Revenue	3.3	4.4	9.0	0.5	17.2
Add back Legacy adjustments from previous price controls included in 2016/17 Regulated Revenue	(0.1)	1.1	(1.6)	(4.3)	(4.9)
Add in Revenue adjustments relating to 2016/17 to be recovered in future years	(5.3)	(9.0)	(2.6)	(2.0)	(19.0)
Allowance for established pension deficit repair payments included in 2016/17 Regulated Revenue	(35.3)	(34.5)	(27.5)	(41.3)	(138.6)
Pass through costs corresponding to amounts included in 2016/17 Regulated Revenue	(44.6)	(51.1)	(26.9)	(27.1)	(149.7)
Network Innovation Allowance costs corresponding to amounts included in 2016/17 Regulated Revenue	(1.6)	(1.6)	(0.8)	(1.1)	(5.1)
LCNF costs corresponding to amounts included in 2016/17 Regulated Revenue	(0.1)	(0.1)	(0.0)	(0.1)	(0.3)
RPI accruals	(1.6)	(1.6)	(0.8)	(1.2)	(5.1)
Other	0.0	(0.2)	(0.1)	0.3	(0.1)
	(114.6)	(64.7)	(58.9)	(82.2)	(320.5)

Pass through costs and adjustments to align revenues includes adjustments to remove amounts included in Regulated Revenue which do not relate to the regulatory year being reported, and add in deferred revenue which relates to the year being reported but which will be received through future years' Regulated Revenues. Also included in Other regulatory allowances are costs which correspond to amounts included in Regulated Revenue. For Pass through costs and Established pension deficit repair payments, these costs are subject to a true-up through the licence agreement, and any differences between allowances and actual costs are held on the balance sheet as they will be recovered through future Regulated Revenues. For LCNF and NIA costs, where a true-up arrangement does not exist, any such differences are reported as under/outperformance within Output incentives earned in the year in the Statement of Financial Performance. See note 3 for further details.

3. Incentives earned

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
Totex incentives for the year	(25.8)	(9.7)	7.2	(19.2)	(47.5)
Less Fast Money element	5.2	1.9	(1.4)	3.8	9.5
Less Enduring Value adjustments	9.5	7.7	6.7	10.6	34.6
Totex incentive value earned (Slow Pot only, net of Enduring Value adjustments)	(11.1)	(0.1)	12.5	(4.7)	(3.4)
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
Interruptions Incentive Scheme (IIS)	19.2	18.5	5.1	3.7	46.4
Broad Measure & Time to connect	6.8	7.3	3.4	5.2	22.7
Guaranteed standards, ex-gratia and fines & redress payments	(0.0)	(0.0)	(0.0)	(0.1)	(0.1)
Losses discretionary reward	0.0	0.0	0.0	0.0	0.2
Low Carbon Network Fund	(0.0)	(0.1)	(0.0)	(0.3)	(0.4)
Network Innovation Allowance	0.0	0.0	0.0	0.0	0.0
Output incentives earned in the year	26.0	25.8	8.5	8.5	68.8

4. Reconciliation of Total Earned Regulatory Revenue to Statutory Accounts

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
Regulated Distribution Network Revenue	495.9	481.8	239.9	356.1	1,573.7
Add: Other turnover items					
Legacy Metering Equipment charges	2.2	3.5	1.1	2.5	9.3
Directly Remunerated Services (DRS) revenue	61.4	64.9	37.1	38.7	202.1
De Minimis Business of the licensee	2.4	3.7	2.2	3.9	12.2
Other adjustments:					
Items reported as Cost Recoveries in OFGEM reporting, but Turnover in the Stat Accounts	4.2	4.1	1.6	2.7	12.6
Items reported as Cost Recoveries in the Stat Accounts, but Revenue in the OFGEM Revenue Return	(0.3)	(0.9)	(0.4)	(0.6)	(2.2)
NIA and LCNF income adjustments	(1.7)	(1.6)	1.7	(1.2)	(2.7)
Connections Contributions reported as DRS revenue but not Turnover in the Stat accounts	(48.5)	(54.0)	(32.0)	(29.9)	(164.4)
Turnover per Statutory Accounts	515.6	501.5	251.2	372.2	1,640.5

2016/17 Notes to Financial Statements

20

5. Analysis of Actual Total Expenditure (Totex)

	Comments	WMID	EMID	SWALES	SWEST	WPD
		£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17	£m 2016/17
Actual load-related capex expenditure	(i)	(18.0)	(33.9)	(3.7)	(10.7)	(66.3)
Actual non-load related capex expenditure - asset replacement	(ii)	(100.8)	(97.0)	(51.7)	(94.6)	(344.2)
Actual non-load related capex - other	(iii)	(14.9)	(15.2)	(8.1)	(13.5)	(51.8)
Actual faults expenditure	(iv)	(40.0)	(36.9)	(12.0)	(25.9)	(114.7)
Actual tree cutting	(v)	(18.2)	(8.8)	(8.2)	(12.5)	(47.7)
Actual 100% 'revenue pool' expenditure	(vi)	(29.6)	(26.5)	(18.8)	(30.1)	(105.0)
Actual controllable opex expenditure	(vii)	(98.3)	(97.3)	(47.9)	(73.1)	(316.6)
Totex		(319.9)	(315.6)	(150.3)	(260.5)	(1,046.3)
Capitalisation rate		80%	80%	80%	80%	80%
Totex Capitalised (Slow money)		(255.9)	(252.5)	(120.3)	(208.4)	(837.1)
Residual: Fast money		(64.0)	(63.1)	(30.1)	(52.1)	(209.3)
Overall Totex		(319.9)	(315.6)	(150.3)	(260.5)	(1,046.3)
Totex		(319.9)	(315.6)	(150.3)	(260.5)	(1,046.3)
Totex allowances		(283.1)	(301.7)	(160.6)	(233.2)	(978.5)
Underspend / (Overspend)		(36.8)	(13.9)	10.2	(27.4)	(67.8)
Incentive rate		70%	70%	70%	70%	70%
Totex incentive gain / (penalty)		(25.8)	(9.7)	7.2	(19.2)	(47.5)
<i>Analysed as:</i>						
Addition in RAV		(20.6)	(7.8)	5.7	(15.3)	(38.0)
Fast money gain		(5.2)	(1.9)	1.4	(3.8)	(9.5)
Totex incentives for the year		(25.8)	(9.7)	7.2	(19.2)	(47.5)
Adjustment for enduring value		9.5	7.7	6.7	10.6	34.6
Net Totex incentives		(16.2)	(2.0)	13.9	(8.5)	(12.9)

Note that the Fast money element of the Totex incentive penalty of -£9.5m above is implicit in the recognition of actual fast pot costs in the Statement of Regulatory Financial Performance. Therefore, only the -£38.0m slow pot element of the penalty, net of £34.6m Enduring Value adjustments, is presented as the -£3.4m Totex incentive penalty incurred in the Statement of Regulatory Financial Performance on page 15.

Totex generally consists of all expenditure relating to a licensee's regulated activities, with a few specific exceptions. It can be summarised as the aggregate net network investment, net network operating costs and indirect costs, less the cash proceeds of sale of assets and scrap.

As part of the RII0 ED1 price control DNOs benefit or are penalised under the **Totex Incentive Mechanism (TIM)**. Under the TIM, WPD retains/bears 70% of any under/over spend on Totex. WPD's **Post-TIM Totex** is equal to the original Totex allowance minus/plus the other 30% of any under/over spend.

Totex is recovered via Fast or Slow pot mechanisms. **Fast pot costs** represent 20% of Totex and are recovered in base revenue in the year incurred. **Slow pot costs** represent 80% of Totex and are added to the RAV balance. Slow pot costs are recovered over future years through RAV depreciation allowances.

Comments:

- (i) Activities include network reinforcement and new connections within the price control.
- (ii) Activities include asset replacement and diversions projects that are not related to additional load requirements on the network.
- (iii) Other capex activities not dependant on additional load requirements on the network or relating to asset replacement capex activities; this includes items such as operational and non-operational IT & telecoms, property and vehicle costs.
- (iv) Expenditure to resolve network faults to ensure supplies are restored as quickly and efficiently as possible.
- (v) An activity required to reduce the likelihood of faults associated with trees being too close to our overhead power lines.
- (vi) This category comprises pension costs associated with regulated business activities.
- (vii) Activities include network inspection, repair and maintenance, closely associated indirect costs and business support costs required to support the management of the network.

2016/17 Notes to Financial Statements

21

6. Analysis of Net Debt

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>
£250m 6.00% bonds 2025	(247.8)				(247.8)
£800m 5.75% bonds 2032	(789.8)				(789.8)
£400m 3.875% bonds 2024	(395.8)				(395.8)
£250m 6.25% bonds 2040		(245.2)			(245.2)
£700m 5.25% bonds 2023		(701.7)			(701.7)
£140m (2016: £100m) 2.671% indexed linked bonds 2043		(196.2)			(196.2)
£105m 1.676% indexed linked bonds 2052		(127.0)			(127.0)
£100m 0.4975% indexed linked bonds 2026		(101.6)			(101.6)
£150m 9.25% Eurobonds 2020			(149.6)		(149.6)
£225m 4.804% bonds 2037			(220.3)		(220.3)
£200m 5.75% bonds 2040			(197.3)		(197.3)
£50m 0.10% indexed linked bonds 2029			(52.6)		(52.6)
£250m 5.875% bonds 2027				(248.4)	(248.4)
£200m 5.75% bonds 2040				(197.3)	(197.3)
£105m 1.541% index linked bonds 2053				(139.2)	(139.2)
£120m 1.541% index linked bonds 2056				(159.1)	(159.1)
Short term borrowings, bank loans and overdrafts		(125.0)		(105.4)	(230.4)
External Debt reported in the Statutory Accounts	(1,433.4)	(1,496.7)	(619.8)	(849.4)	(4,399.3)
Add:					
Intercompany loans	(2.5)	(8.9)	0.0	(7.7)	(19.1)
Cash and cash equivalents	11.5	11.4	19.5	21.7	64.0
Other amounts due to/(from) group companies	24.8	5.7	16.8	(64.9)	(17.5)
OFGEM definition of Total Net Debt per Statutory Accounts	(1,399.6)	(1,488.5)	(583.5)	(900.3)	(4,371.9)
Less:					
Unamortised issue costs	(5.5)	(5.0)	(6.6)	(2.3)	(19.4)
(Discount)/premium on issue	(11.1)	53.4	1.5	(2.3)	41.6
Less: Long term loans to related parties that are not distributions or for the benefit of the Regulated Business	0.0	0.0	0.0	(1.2)	(1.2)
Other amounts due to/(from) group companies	(24.8)	(5.7)	(16.8)	64.9	17.5
Regulatory Net Debt	(1,441.0)	(1,445.8)	(605.4)	(841.2)	(4,333.4)

2016/17 Notes to Financial Statements

22

Summary of Regulatory Net Debt movements	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>
Opening regulatory net debt	(1,329.4)	(1,356.4)	(600.3)	(806.3)	(4,092.4)
Revenue within price control	495.9	481.8	239.9	356.1	1,573.7
LCNF successful delivery reward and IIS penalty protection award	0.0	0.0	2.5	0.0	2.5
Actual Totex expenditure	(319.9)	(315.6)	(150.3)	(260.5)	(1,046.3)
Pass through costs	(43.3)	(51.1)	(28.3)	(25.7)	(148.4)
Established Pension Deficit Funding, Cash payment	(68.1)	(66.6)	(55.7)	(84.5)	(274.9)
NIA, NIC and LCNF	(2.0)	(1.8)	(0.8)	(1.6)	(6.2)
Disallowed Related Party Margin and DRS 8 Revenue	(2.5)	(3.6)	(1.6)	(3.3)	(11.0)
Other Regulatory adjustments	0.9	1.2	4.4	(15.3)	(8.8)
Activities using assets outside RAV, Revenue	17.5	18.1	8.4	15.1	59.1
Activities using assets outside RAV, Net additions	2.7	4.1	(2.6)	(1.3)	2.9
Activities using assets outside RAV, Costs	(16.8)	(15.8)	(7.3)	(9.4)	(49.3)
Non-Regulated Pension Deficit Funding, Cash payment	(16.5)	(16.1)	(13.0)	(19.7)	(65.3)
Movement in inventory	(0.2)	(1.9)	(0.2)	(1.0)	(3.3)
Movement in creditors	(18.6)	(6.9)	(6.9)	22.9	(9.5)
Movement in debtors	(14.1)	11.4	(3.5)	(5.4)	(11.6)
Movement in provisions, advance capital contributions, capital accruals	3.0	(10.3)	3.7	1.2	(2.4)
Interest received	0.5	0.1	0.0	3.3	3.9
Interest paid	(76.7)	(57.5)	(36.1)	(32.6)	(202.9)
Valuation movements (e.g. indexation)	0.0	(7.6)	0.2	(7.5)	(15.0)
Tax paid	(17.8)	(18.2)	(0.8)	(16.2)	(53.0)
New debt - removal of premium (net of historic accretion)	0.0	36.9	2.9	0.0	39.7
Dividends received	0.1	0.1	0.0	0.0	0.2
Dividends paid	(90.8)	(130.0)	0.0	(24.4)	(245.2)
Issue share capital	55.0	60.0	40.0	75.0	230.0
Closing Regulatory Net Debt	<u>(1,441.0)</u>	<u>(1,445.8)</u>	<u>(605.4)</u>	<u>(841.2)</u>	<u>(4,333.4)</u>

The RIIO accounts use Regulatory Net Debt, which is OFGEM's definition of Net debt, as set out in OFGEM's 31 July 2009 tax clawback open letter. OFGEM uses the Regulatory Net Debt position to assess a DNO's gearing level against the OFGEM notional gearing level. It should be noted that data reported to OFGEM also includes a presentation of Net Debt per the Statutory Accounts. WPD's DNOs' statutory accounts include the definition of External Debt shown above. This table shows the reconciliation between these definitions. The notional gearing level for RIIO ED1 is 65%. Should actual gearing exceed 65% then OFGEM, via an annual tax clawback mechanism, requires DNOs to return any financial benefit gained from lower tax costs associated with higher gearing levels.

2016/17 Notes to Financial Statements

23

7. Return on Regulatory Equity (RoRE)

WMID

EMID

SWALES

SWEST

WPD

WPD presented the following analysis of Forecast ED1 Total RoRE to OFGEM in its 2016/17 Strategic Performance Overview pilot document:

	Comments	Forecast		Forecast		Forecast		Forecast		Forecast	
		2016/17	ED1 Total	2016/17	ED1 Total						
Cost of Equity	(i)	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%
TIM Retained Proportion	(ii)	-3.4%	-0.6%	-1.3%	0.4%	2.1%	1.4%	-4.0%	0.5%	-2.1%	0.3%
IQI Additional Income	(iii)	0.7%	0.7%	0.8%	0.7%	1.0%	0.9%	1.0%	0.9%	0.8%	0.8%
Broad Measure of Customer Service	(iv)	0.6%	0.6%	0.6%	0.6%	0.7%	0.6%	0.7%	0.6%	0.6%	0.6%
Interruptions Related Quality of Service	(v)	2.1%	2.0%	2.0%	1.7%	1.2%	1.1%	0.6%	0.6%	1.6%	1.5%
Time to Connect Incentive Revenue	(vi)	0.1%	0.1%	0.2%	0.2%	0.2%	0.1%	0.2%	0.2%	0.2%	0.2%
Losses Discretionary Reward Scheme	(vii)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Tax Allowance Retained Within Deadband	(viii)	0.0%	0.1%	0.0%	0.1%	0.0%	0.1%	0.0%	0.1%	0.0%	0.1%
RoRE Total		6.5%	9.4%	8.7%	10.2%	11.6%	10.6%	4.9%	9.3%	7.6%	9.8%
Regulatory Equity used; 35% NPV Neutral RAV Return Base (£m)		754.8	784.6	750.8	778.2	329.2	359.8	482.4	530.4	2,317.2	2,453.0

Comments:

- (i) This is the cost of equity set for RIIO ED1
- (ii) Totex Incentive Mechanism (TIM) element retained/(borne) by the DNO.
- (iii) Income associated with OFGEM awarding WPD 'Fast Track' status for business plans deemed to be of particularly high quality, efficient and value for money.
- (iv) to (vii) Income associated with output/performance incentives to drive improved customer service, connections and quality of service for supply interruptions.
- (viii) Benefit received from UK tax rate changes that are within the DNO's tax allowance dead band.

Only the ED1 Total RoRE from the analysis above was presented in the 2016/17 Strategic Performance Overview. This comprised the above values in the 2016/17 column, plus actual values for 2015/16 and forecast values for the remaining ED1 years. This RoRE calculation aligns with OFGEM's presentation in the ED1 Annual Report, although the values differ slightly due to WPD using different assumptions from OFGEM in some areas.

The NPV Neutral RAV Return Base (NNRRB) is the arithmetic average of the opening and discounted closing RAV balance for the year, and is calculated in the PCFM.

2016/17 Notes to Financial Statements

24

Using the information in these RIIO accounts, an extended RoRE for the 2016/17 Regulatory Year is calculated below. The outlined 2016/17 values are comparable to the 2016/17 values outlined in the analysis on page 23.

		WMID			EMID			SWALES			SWEST			WPD		
		RoRE £m from SOFP	RoRE % using Reg Equity from SOFP	RoRE % using NNRRB * 35%, as above	RoRE £m from SOFP	RoRE % using Reg Equity from SOFP	RoRE % using NNRRB * 35%, as above	RoRE £m from SOFP	RoRE % using Reg Equity from SOFP	RoRE % using NNRRB * 35%, as above	RoRE £m from SOFP	RoRE % using Reg Equity from SOFP	RoRE % using NNRRB * 35%, as above	RoRE £m from SOFP	RoRE % using Reg Equity from SOFP	RoRE % using NNRRB * 35%, as above
Net allowances for the cost of equity	(i)	48.3	5.5%	6.4%	48.0	6.2%	6.4%	21.1	4.6%	6.4%	30.9	4.7%	6.4%	148.3	5.4%	6.4%
Totex incentives	(ii)															
Fast money gain/(loss)		(5.2)			(1.9)			1.4			(3.8)			(9.5)		
Slow money gain/(loss)		(20.6)			(7.8)			5.7			(15.3)			(38.0)		
		(25.8)	-3.0%	-3.4%	(9.7)	-1.3%	-1.3%	7.2	1.6%	2.2%	(19.2)	-2.9%	-4.0%	(47.5)	-1.7%	-2.0%
Additional income/IQI	(iii)															
Pre tax		7.1	0.8%		7.5	1.0%		4.0	0.9%		5.8	0.9%		24.4	0.9%	
Less: Tax		(1.4)			(1.5)			(0.8)			(1.2)			(4.9)		
		5.6		0.7%	6.0		0.8%	3.2		1.0%	4.7		1.0%	19.5		0.8%
Output incentives:																
IIS	(v)	19.2			18.5			5.1			3.7			46.4		
Broad Measure & Time to connect	(iv), (vi)	6.8			7.3			3.4			5.2			22.7		
Guaranteed standards, ex-gratia payments and fines & redress payments		(0.0)			(0.0)			(0.0)			(0.1)			(0.1)		
LCNF		(0.0)			(0.1)			(0.0)			(0.3)			(0.4)		
Losses discretionary reward	(vii)	0.0			0.0			0.0			0.0			0.2		
Total output incentives pre-tax		26.0	3.0%		25.8	3.3%		8.5	1.9%		8.5	1.3%		68.8	2.5%	
Less: Tax (at CT rate in year of recovery)		(4.9)			(4.9)			(1.6)			(1.6)			(13.1)		
		21.1		2.8%	20.9		2.8%	6.9		2.1%	6.9		1.4%	55.7		2.4%
RoRE presented above (post-Tax basis)				6.5%			8.7%			11.6%			4.8%			7.6%
Additional items, added to pre-Tax values above:																
Enduring Value adjustment		9.5	1.1%		7.7	1.0%		6.7	1.5%		10.6	1.6%		34.6	1.3%	
Disallowed Related Party margin, DRS 8 Income and removal of NBV of disposals		(2.5)	-0.3%		(3.7)	-0.5%		(1.7)	-0.4%		(3.6)	-0.5%		(11.5)	-0.4%	
Other pre-financing adjustments in Statement of Regulatory Financial Performance		0.6	0.1%		(1.0)	-0.1%		1.1	0.2%		(1.5)	-0.2%		(0.7)	0.0%	
RoRE - Pre-Financing variances		63.3	7.3%		74.6	9.7%		46.9	10.3%		31.6	4.8%		216.4	7.9%	
Financing variances, including income from FA investments		(13.2)	-1.5%		(5.8)	-0.8%		(9.2)	-2.0%		6.8	1.0%		(21.4)	-0.8%	
Other interest and time value of money items		1.6	0.2%		1.3	0.2%		1.8	0.4%		1.2	0.2%		5.8	0.2%	
RoRE before tax variance and return using assets outside the RAV		51.6	5.9%		70.1	9.1%		39.5	8.7%		39.6	6.0%		200.8	7.3%	
Tax variance (including gearing variance)		(7.4)	-0.8%		(10.4)	-1.3%		(6.8)	-1.5%		(8.0)	-1.2%		(32.5)	-1.2%	
RoRE after tax and gearing variance		44.2	5.1%		59.7	7.7%		32.7	7.2%		31.6	4.8%		168.3	6.1%	
Return on activities using assets outside the RAV		(2.4)	-0.3%		(0.6)	-0.1%		3.8	0.8%		10.6	1.6%		11.4	0.4%	
Total RoRE		41.8	4.8%		59.1	7.7%		36.4	8.0%		42.2	6.4%		179.7	6.5%	
Regulatory Equity per Statement of Financial Position (SOFP) (£m)		871.5			771.3			456.1			655.9			2,754.8		

The RoRE values above align with the presentation shown in the alternative Statement of Regulatory Financial Performance, on page 17.

RoRE reflects the financial return achieved by the licensee from its performance under the RIIO ED1 price control framework.

RoRE is calculated post-tax and is estimated using certain regulatory assumptions, such as the assumed gearing ratio of the companies, to ensure comparability across the sector and is expressed as a percentage of regulatory equity.

The aim of the RoRE measure is to provide an indication of the return achieved by the owners of a licensee which can be compared to the cost of equity originally allowed in the price control settlement and to the return achieved by other licensees on an equivalent basis.

Note that the Current tax charge for SWALES has been adjusted in these RIIO accounts to remove the tax benefit from pensions contributions reimbursed by another WPD entity.

2016/17 Notes to Financial Statements

25

8. Regulatory Asset Value (RAV)

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
RAV at 31-Mar-2016 , as previously reported	2,144.3	2,126.0	929.2	1,351.2	6,550.7
Slow money Totex additions	255.9	252.5	120.3	208.4	837.1
RAV uplift/reduction from TIM	(20.6)	(7.8)	5.7	(15.3)	(38.0)
Depreciation	(190.4)	(186.7)	(93.2)	(125.2)	(595.6)
Indexation	72.2	71.9	31.6	46.3	222.0
RAV at 31-Mar-2017	2,261.4	2,255.9	993.5	1,465.4	6,976.2

RAV is a financial balance representing historical expenditure by the licensee that has been capitalised under regulatory rules as determined by OFGEM.

ED1 RAV additions are equal to 80% of post-TIM Totex; RAV additions are depreciated on an annual basis, commencing in the year following the year of investment. Asset life varies dependent upon the year of investment. DNOs also receive a return on RAV, based on a vanilla Weighted Average Cost of Capital (WACC) for the price control (currently 6.4% for WPD).

9. Other regulatory balances

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	2016/17	2016/17	2016/17	2016/17	2016/17
K-factor	(3.4)	(7.5)	1.7	(9.5)	(18.8)
IIS incentive income	41.3	39.9	10.5	9.6	101.4
Broad Measure & Time to connect incentive income	13.9	14.8	6.6	10.3	45.7
Losses discretionary reward	0.0	0.0	0.0	0.0	0.2
Network Innovation Allowance	0.2	0.2	0.1	0.2	0.7
DPCR4 Residual distribution losses incentive	0.0	(16.3)	0.0	0.0	(16.3)
Established pension deficit recovery	80.5	78.5	45.6	63.6	268.2
Deferred Base Revenue accruals	(5.5)	(9.2)	(3.6)	(4.5)	(22.8)
Pass through costs	(2.9)	0.5	5.2	(2.4)	0.4
RPI accruals	(9.9)	(10.0)	(5.1)	(7.4)	(32.4)
Revenue profiling adjustments	12.1	14.2	20.4	(0.5)	46.2
Legacy recoveries from previous price controls	1.2	(7.4)	12.9	34.1	40.8
Other regulatory true ups	6.7	5.7	4.4	5.9	22.7
Enduring value adjustments	9.7	7.7	6.9	10.8	35.1
Provision amounts recoverable	21.3	12.0	9.5	13.6	56.3
	165.1	123.3	115.0	123.9	527.3

Other regulatory balances arise in the RIIO accounts as a result of timing differences between revenue received and revenue earned in the period under the regulatory framework. Revenue is recognised when regulatory activities are performed, rather than when customers have been billed, to the extent that actual expenditure incurred is expected to be recoverable in accordance with the regulatory agreement. Amounts are derecognised when the amounts have been settled or WPD is no longer entitled to recover the amounts.

Enduring value adjustments arise to adjust for intra-period timing differences, to ensure that any under or outperformance which will reverse in future years within the price control is not recognised.

Of the £35.1m total WPD enduring value adjustments above, £35.9m is to reverse the Totex penalty incurred due to inclusion of £50.4m of the £230m pensions prepayment within Totex, which will then reverse in future years when the prepayment is unwound. This is offset by a -£0.8m anticipated adjustment to 2016/17 Totex in EMID. These amounts include indexation of £0.5m which is not included in the Statement of Financial Performance.

Provision amounts recoverable balances are created to offset any atypical provisions, for which any related costs are included within Totex on a cash basis only.

2016/17 Notes to Financial Statements

26

10. Activities outside of RAV

	WMID	EMID	SWALES	SWEST	WPD
	£m	£m	£m	£m	£m
	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>	<u>2016/17</u>
Activities using assets outside the RAV					
Revenues	17.5	18.1	8.4	15.1	59.1
Operating costs	(15.9)	(15.2)	(6.6)	(8.3)	(45.9)
Depreciation and amortisation	(3.5)	(3.8)	(0.3)	(2.1)	(9.7)
Revaluation movement on the non-regulatory element of defined benefit pensions	(0.5)	0.4	2.2	5.8	7.9
Return on activities using assets outside the RAV	(2.4)	(0.6)	3.8	10.6	11.4
Fixed assets: activities using assets outside the RAV					
Book Value at 31-Mar-2016	8.6	(0.7)	1.9	5.2	14.9
Net additions to/(disposal of) fixed assets	(2.7)	(4.1)	2.6	1.3	(2.9)
Depreciation and amortisation	(3.5)	(3.8)	(0.3)	(2.1)	(9.7)
Book value at 31-Mar-2017	2.4	(8.7)	4.1	4.4	2.3

Activities outside the RIIO ED1 price control form part of a DNO's licence conditions but are not billed via the Distribution Use of System (DUoS).

Activities include Connections (Sole use, 100% funded by customers), Directly Remunerated Services (Diversion, Service alterations), De Minimis (Multi utilities gas/water, property rentals and private networks), and Meter activities.

11. Further reconciliations to Statutory Accounts and other documents

WPD has not provided any further reconciliations between these RIIO accounts and the Statutory Accounts but welcomes feedback from stakeholders if they consider further reconciliations would be helpful.

A reconciliation of total costs reported to Ofgem in the Regulatory Reporting Pack to the Regulatory Accounts is included in WPD's regulatory submissions to OFGEM.

Note that, as WPD has a 31 March year-end, the Statutory Accounts and the Regulatory Accounts for the four companies reported contain the same results. Reconciliations to the Statutory Accounts above therefore equally apply to the Regulatory Accounts.

Western Power Distribution Sources

WPD website	http://www.westernpower.co.uk/
Summary of WPD's 2016/17 Business Plan Commitment Report	https://www.westernpower.co.uk/docs/About-us/Stakeholder-information/Performance-reporting-RIIO-ED1/2017/Summary-Report-Business-Plan-Commitments-Report-20.aspx
Detailed 2016/17 Business Plan Commitment Report	https://www.westernpower.co.uk/docs/About-us/Stakeholder-information/Performance-reporting-RIIO-ED1/2017/WPD-RIIO-ED1-Business-Plan-Commitments-Report-2016.aspx
WPD RIIO ED1 business plan	https://www.westernpower.co.uk/docs/About-us/Stakeholder-information/Our-future-business-plan/WPD-RII-ED1-Business-Plan/WPD-RIIO-ED1-Business-Plan.aspx

External Sources

OFGEM website	https://www.ofgem.gov.uk/
RIIO ED1 price control information	https://www.ofgem.gov.uk/network-regulation-riio-model/riio-ed1-price-control
OFGEM's RIIO ED1 Price Control Financial Model (PCFM)	https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-financial-model-following-annual-iteration-process-2017
RIIO ED1 Annual Report 2016/17	https://www.ofgem.gov.uk/system/files/docs/2017/12/riio-ed1_annual_report_2016-17.pdf
OFGEM 31st July 2009 tax clawback open letter	https://www.ofgem.gov.uk/ofgem-publications/42857/taxclawbackopenletter-july09.pdf
WPD's Electricity Distribution Licence	https://epr.ofgem.gov.uk//Content/Documents/Electricity%20Distribution%20Consolidated%20Standard%20Licence%20Conditions%20-%20Current%20Version.pdf

Western Power Distribution (East Midlands) plc number 2366923

Western Power Distribution (West Midlands) plc number 3600574

Western Power Distribution (South West) plc number 2366894

Western Power Distribution (South Wales) plc number 2366985

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