Scottish Hydro Electric Power Distribution plc

Directors Report and Financial Statements

Year ended 31 March 2021

Registered No.: SC213460

Scottish Hydro Electric Power Distribution plc

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Directors and Other Information

Directors	Gregor Alexander (Non-Executive Director) (Chairman) Colin Nicol (Resigned 04/01/21) Rob McDonald Chris Burchell (Appointed 04/01/21) Eliane Algaard (Appointed 01/09/20) Mark Rough (Appointed 01/04/20) Sandy MacTaggart (Appointed 23/02/21) Maz Alkirwi (Appointed 23/02/21) Rachel McEwen (Non-Executive Director) Katherine Marshall (Non-Executive Director) David Rutherford (Independent Non-Executive Director) Gary Steel (Independent Non-Executive Director)
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Registered number	SC213460

Scottish Hydro Electric Power Distribution plc

Strategic Report

The Strategic Report sets out the main trends and factors underlying the development and performance of Scottish Hydro Electric Power Distribution plc (the "Company") during the year ended 31 March 2021, as well as those matters which are likely to affect its future development and performance.

The business, its objectives and strategy

The Company is a wholly owned subsidiary of SSE plc (the "Group"). The Company's immediate parent is Scottish and Southern Energy Power Distribution Limited (SSEPD) which is branded as Scottish and Southern Electricity Networks (SSEN). Included within the SSEN group are sister companies, Scottish Hydro Electric Transmission plc (SHET) and Southern Electric Power Distribution plc (SEPD). The Company distributes electricity to around 740,000 (2020: 740,000) customers in the north of Scotland. It currently has over 50,000 (*2020: 49,000*) kilometres of electricity mains on commission. The Company also provides electricity connections within the Company's licensed area and owns and operates a number of the out of area electricity networks in the rest of Scotland.

The Company is the subject of incentive-based regulation by the industry regulator, the Office of Gas and Electricity Markets (Ofgem), which sets the prices that can be charged for the use of the electricity network, the allowed capital and operating expenditure, within a framework known as the Price Control. In broad terms, Ofgem seeks to strike the right balance between attracting investment in electricity networks, encouraging companies to operate the networks as efficiently as possible and ensuring that prices for customers are no higher than they need to be. Ofgem also places specific incentives on companies to improve their efficiency and quality of service. The Company is currently within the RIIO-ED1 (Revenue = Incentives + Innovation + Outputs) Price Control period which runs for eight years from 1 April 2015 until 31 March 2023.

The Company's strategy and main objectives are to:

- comply fully with all electricity network safety standards and environmental requirements;
- ensure that the electricity network is managed as efficiently as possible, including maintaining tight controls over operational expenditure;
- provide good performance in areas such as reliability of supply, customer service and innovation and thus earn additional incentive-based revenue under the various Ofgem schemes;
- deliver efficient and innovative capital expenditure programmes, so that the number and duration of power cuts experienced by customers is kept to a minimum;
- grow the Regulated Asset Value ("RAV") of the business and so secure increased revenue;
- engage constructively with the regulator, Ofgem, to secure regulatory outcomes that meet the needs of customers and investors; and
- engage with the wider networks industry and other stakeholders to define and implement the process of distribution companies moving to a Distribution System Operator (DSO) role.

Business performance overview

The key performance indicators of the Company and the related performance during the year to 31 March 2021 were as follows:

Financial / Operational	**2021**	2020
Reported Operating Profit - £m	**98.8**	100.0
Exceptional restructuring costs - £m	**-**	1.7
Derivative re-measurements - £m	**(3.9)**	7.4
Adjusted Operating Profit - £m	**94.9**	109.1
Capital expenditure - £m	**133.2**	126.2
Regulated asset value (RAV) - £m	**1,238.8**	1,191.5

Non-Financial / Management	**2021**	2020
Customer Minutes Lost - number per customer	**57**	56
Customer Interruptions - number per 100 customers	**64**	63
Electricity distributed (TWh)	**6.8**	7.3

Business performance overview *(continued)*

The performance of the Company is considered on adjusted operating profit which excludes non-recurring exceptional restructuring costs and re-measurements arising from operating derivatives.

The Company is exposed to market risk on commodity derivatives, associated with fluctuations in the market price of oil which can cause volatility on revaluation. The Company's adjusted operating profit measure excludes this mark-to market movement as it is not relevant in assessing underlying performance.

The adjusted operating profit has decreased by 13% to £94.9m in the year. This is attributable to an increase in distribution costs relating to the impact of national and regional lockdowns and increased depreciation charges driven by prior year capital investment. In the prior year, reported operating profit included a non-recurring £1.7m exceptional charge for restructuring expenses which has been fully utilised in the year. In 19/20 the Company also experienced a £7.4m commodity derivative loss. The commodity derivative expired in December 2020 and was replaced with a new oil option contract which generated a £1.3m gain in the year. The prior year exceptional item relates to a non-recurring restructuring programme which was undertaken in 2020.

If in any year, regulated network companies' revenue is greater (over recovery) or lower (under recovery) than is allowed under the ED1 Price Control, the difference is carried forward and the subsequent prices the companies may charge are adjusted. Under the regulatory framework, distribution tariffs are set two years in advance which means the over/under recovery built into tariffs is a forecast and will differ from the actual outturn. Any difference is reflected in tariffs two years later meaning any difference in the 2020/21 forecast compared to actual will be fully unwound through revenue by 2025, making this in essence a four year cycle. The phasing of changes in tariffs and volumes between reporting periods has meant an over-recovery of £5.4m in 2019/20 was replaced with a £14m over-recovery in 2020/21.

During the year, the Company's Customer Minutes Lost (CML) increased from 56 to 57 minutes per customer and Customer Interruptions (CI) increased from 63 to 64 per 100 customers. The Company continues to outperform the pre-determined targets set by Ofgem.

Volume of electricity distributed

The total volume of electricity distributed by the Company during 2020/21 was 6.8TWh, compared with 7.3TWh in 2019/20. Under RIIO-ED1, the volume of electricity distributed does not affect the Company's overall allowed revenue. This only has an impact on the timing of revenue collection as any over or under recovery which arises as a result will not be fully unwound until four years later, as described above.

Delivering for customers and investors under the incentive based framework

Two years remain of the RIIO-ED1 Price Control and the Company continues to deliver significant changes to its operations, processes and standards to ensure the needs of its customers remain at the forefront of decision making. It aims to be as efficient and effective as possible and earn returns that are fair to customers and shareholders alike, focusing on four key areas:

- Good performance in relation to incentives available within RIIO-ED1;
- Efficient delivery of capital investment;
- Focused delivery of regulatory outputs; and
- Maintaining a leadership position in innovation.

Incentive performance in 2020/21 is expected to be £4.7m on finalisation, compared to £4.8m in 2019/20. This represents a slight decrease on prior year and improving performance in this area is a key focus for the year ahead. There was improved incentive performance under the Average Time to Connect (TTQ/TTC), Customer Satisfaction Scheme (Broad Measure) and Stakeholder Engagement and Consumer Vulnerability incentives, which was offset by a drop in performance under the Interruptions Incentive Scheme (IIS). Typically, incentive income is collected two years after the performance year.

The Company is also shaping its future and has published its draft business plan for the next regulatory period RIIO-ED2 (2023-2028). Informed by an extensive stakeholder engagement programme, the plan will support a cost effective and secure path to net zero for customers and communities while representing a fair financial package for investors that recognises current and future demand and risk.

Targeting performance in interruption incentives

Under the IIS, the Company is incentivised on its performance against the loss of electricity supply through the recording of CI and CML, which include both planned and unplanned supply interruptions.

The Company achieved an incentive award of £0.9m in 2020/21, which is a decrease on the £1.5m achieved in 2019/20. The decrease has been driven by the challenges posed by the worst weather conditions in over a decade in the North of Scotland. The Company continues to assess the enabling of swift and efficient restoration of power supplies to customers, alongside network investment.

Delivering for customers and stakeholders

In 2020/21, the Company's focus on continual improvements in customer service resulted in a total incentive reward of £2.45m against Customer Satisfaction Incentive (Broad Measure), a slight increase from £2.4m in the previous year. This reflects a strong performance amidst the challenges during COVID lockdown and recovery, particularly in the Company's license area. The Company is achieving this through a targeted improvement programme which drives improved communication with customers, providing advanced notice and accurate information to customers.

An increased reward of £0.4m was secured from the Stakeholder Engagement and Consumer Vulnerability incentive relating to financial year 2019/20, representing the Company's best return since 2016/17.

Driving value from connections

The customer-focused improvements the Company has implemented in its connections business continues to deliver consistent high performance, reflected by the award of £1.0m under the Average Time to Connect (TTC) Incentive for 2020/21. This is aligned with performance last year where the Company also received a reward of £1.0m.

Ofgem announced its decision not to penalise the Company under the penalty only Incentive on Connections Engagement (ICE). This is the fifth consecutive year the Company has avoided a penalty since its introduction at the beginning of the RIIO-ED1 Price Control period.

In line with the RIIO-ED1 regulatory settlement, incentive targets have become harder to achieve in the second half of the price control, but the Company remains confident that it will deliver sustained incentive performance in this area.

Operational delivery

Key to successful delivery against any regulatory price control is efficient and focused capital investment, upgrading and expanding the infrastructure critical to support the net zero transition. In 2020/21, the Company continued its major capital investment programme, delivering significant improvements for customers and increasing Regulated Asset Value (RAV).

During 2020/21, the Company's RAV additions and hence investment in the electricity distribution network was £134.8m, bringing the total RAV additions since the beginning of the RIIO-ED1 Price Control to over £0.7bn. This included a £10m programme of investment in Aberdeen to upgrade the underground network and install automation capability.

As part of its 'flexibility first' approach to network investment, the Company continues to secure flexible energy service contracts with the objective of powering an increasing amount of homes. This will increasingly play a vital role in supporting the delivery of a smarter electricity grid and a cost-effective transition to net zero.

Growth Opportunities

Achieving the UK's net zero ambitions will require extensive electrification of heat and transport and it is crucial that the local electricity distribution networks act as an enabler not a constraint to this significant change. The Company strongly supports a mechanism for strategic investment in flexible solutions or network reinforcement to enable a cost-effective transition to net zero for the households, businesses and communities it serves.

Growth Opportunities *(continued)*

In support of this aim and the Government's green recovery ambitions, the Company alongside other SSEN companies partnered with the Energy Networks Association (ENA), DNO licensees and Ofgem to develop a targeted Green Recovery investment programme. Following a six week stakeholder consultation to identify 'shovel-ready' low-carbon projects that could be unlocked by early investment in the network, 12 network schemes were proposed representing £41m of additional investment during the current price control period. This expenditure will be incurred outside of the totex (total expenditure) investment mechanism, delivering additional value for shareholders, subject to final approval from Ofgem.

To understand the growth potential of electrification for SSEN's distribution networks, updated Distribution Future Energy Scenario reports were published in December 2020. The upper range of the net zero scenarios forecasts the number of electric vehicles, heat pumps and local renewable capacity in SSEN Distribution licence areas, for which the Company's license area spans a large proportion, to increase significantly from 2020 to 2050.

This analysis is one of the factors which has informed the Company's draft RIIO-ED2 business plan submission. Co-created with stakeholders and customers, the ambitious plan will deliver targeted investment in network resilience to build a foundation for an electrified future, improvements to the valued service for customers and communities and further development of the smart, flexible, local energy networks to accelerate progress to net zero. While it is too early for specific projections, an increase in investment on ED1 rates is needed to meet customer needs and keep pace with net zero policy and targets.

Helping accommodate the national roll-out of electric vehicles

Collaboration has been key in 2020/21, with the Company moving ahead on innovation projects with partners to support flexible markets and future infrastructure provision for the mass adoption of electric vehicles (EVs).

Major innovation projects have included Optimise Prime, a fleet electrification project which has moved into physical trials; and Skyline, a first-of-its-kind project launched in 2020/21, which will establish data sharing with the automotive and charge point industries to allow early visibility of planned domestic EV charger connections. The Company is also a core member of the Scottish Government's Strategic EV Partnership.

Planning for RIIO – ED2

The Company has submitted its draft business plan for the next electricity distribution price control period, RIIO-ED2, which will run from 2023-2028. The draft plan sets out how the Company will deliver improvements for customers and accelerate investment in its networks to power communities to net zero.

In February 2021, the Company published its Blueprint for RIIO-ED2, Shaping a sustainable energy future. This document helped provide stakeholders with a solid platform of understanding from which it could explore specific challenges, topics, or regional issues that may be of interest. A microsite was also developed, while a variety of events were held with stakeholders, both at a local and a national level.

The stakeholder-led plan balances the need to accelerate investment in the smart and flexible electricity networks that will meet new decarbonisation demands, while keeping costs down for consumers. It also responds to stakeholder feedback, proposing improvements to service, increased reliability and resilience; and support for those most vulnerable, particularly in the light of the ongoing social and economic impact of Covid-19.

Co-created through three phases of enhanced engagement with its stakeholders, the RIIO-ED2 business plan sets out six clear goals that the Company will deliver for customers and communities, alongside its sister company, SEPD, by 2028:

- Reduce the frequency and duration of unplanned power interruptions by 20%;
- Create a foundation for net zero by investing £1bn in strategic resilience across its networks;
- Achieve a customer satisfaction score of 9.2 or more (out of 10) in every customer contact area;
- Support 200,000 customers in vulnerable situations with targeted fuel poverty, personal resilience or energy efficiency measures;
- Facilitate the connection of an additional 1.3 million electric vehicles and 800,000 heat pumps; and
- Reduce its business carbon footprint by at least 35%, aligned to a 1.5c science-based target.

Planning for RIIO – ED2 (*continued*)

The draft base plan aims to deliver these goals and increased investment with no planned rise in network charges on customer energy bills, supporting a just and fair transition to net zero. This will be achieved through the efficiency savings and innovation, coupled with lower financing costs.

The development of the Company's ED2 plan has been a continuous conversation and the Company will continue to gather feedback from customers and stakeholders and to refine the details of the plan before December this year.

Impact of Coronavirus

Coronavirus has had a significant impact across the economy in the UK and Ireland and as expected the pandemic has caused greater challenges for the Company's Distribution business. The impact on operating profit was slightly below that anticipated which is mainly due to better than expected demand.

The pandemic has principally impacted the Company's use of system (DUoS) revenue, for which it is estimated that around £12m was lost to the virus as a result of reduced customer demand.

Additional modelling and future forecasting has been undertaken by the Company in order to consider sensitivities to future profitability and financing as a result of the pandemic together with the impact this could have on the Company's going concern. This is referred to in the Corporate Governance Statement and the Company's Viability Statement on pages 19 and 20.

Electricity Distribution priorities

The Company's priorities in 2021/22 and beyond are to:

- operate safely and meet all compliance requirements;
- provide an excellent service to all customers who rely on their networks and related services;
- deliver required outputs while maintaining tight controls over expenditure;
- maintain good progress in the safe delivery of new assets including submarine cables;
- continue to work with stakeholders in developing a sustainable long term energy solution for Shetland;
- progress innovations that will improve network reliability, efficiency and customer service and inform industry-wide improvements;
- develop and maintain effective stakeholder relationships and conduct constructive engagement with regulators and legislators, advocating clarity and stability in the regulatory framework including getting ready for RIIO-ED2; and progress the transition towards operating in a DSO environment.

Values and responsibilities

The Group and the Company believe that the behaviours and culture of an organisation should be guided by its values, and that an organisation's values should be at its core. The Group has six core values which seek to bind the behaviour and attitude of its employees and those it works with. They are:

- Safety: If it's not safe, we don't do it;
- Service: We are a company customers can rely on;
- Efficiency: We focus on what matters;
- Sustainability: We do things responsibly to add long-term value;
- Excellence: We continually improve the way we do things; and
- Teamwork: We work together, respect each other and make a difference.

Scottish Hydro Electric Power Distribution plc

Strategic Report *(continued)*

Understanding and managing our principal risks

To help ensure it is able to provide the energy people need and deliver value over the long term, the Group has continued to develop its Risk Management Framework, including its Principal Risks and its Risk Appetite Statement. For further detail on how the Group manages risk see the published SSE Group Risk Report and the Risk Management Frameworks section in the SSE plc Annual Report (www.sse.com).

The Group Risk Management Policy requires the Managing Director of each Business Unit to implement a Divisional Risk Approach to support their business in identifying, understanding and managing its key risks. Each division carries out an annual Assurance Evaluation with key Group policies, with the output and any areas of required improvement reported to the Group's Chief Executive.

The risks faced by the Company have been considered by the Board during the financial year. These have been reviewed in line with the Group's approach to risk. Risk workshops have been attended by the Distribution Executive Committee and Company's Board members during the year in order to aid identification of the risks specific to the business. As a result of this process, the main risks were identified which have the potential to threaten the business model, future performance, solvency or liquidity of the Company. An overview of these risks and the mitigating actions are as follows:

- **Safety, Health and Environment** – The Company's operations are in many cases undertaken in hazardous environments and involve working with high voltage electricity in a wide variety of locations. Some of our operations require the storage of a significant volume of fuel, oil and other chemicals, and any uncontrolled release of these could result in injury to our staff, contractors or members of the public and damage to the environment. Safety is the number one value and priority for the Group and Company. There is a Safety Management System in place to support people at work and ensure their safety and significant focus on both technical and behavioural safety training. In addition, crisis management and business continuity plans are in place to manage and recover from any significant events.
- **Political and Regulatory Change** – Our business continues to be subject to political, regulatory and legislative demands and changes. The Political and Regulatory Engagement Policy is supported by a Communication, Regulation and Stakeholder Engagement Directorate which directly manages the political engagement for the Company with key political stakeholders, while maintaining a healthy and ongoing relationship with the regulator. In addition to this, a RIIO-ED2 works to develop and deliver a robust regulatory plan.
- **Legislative and Regulatory Compliance** – Regulation, legislation and compliance affecting the Company is complex and fast-moving. Changes, either explicit or indirect, can lead to additional obligations and can have a significant effect on the profitability of our asset base. This risk is mitigated jointly by Company management and staff along with the Group's dedicated Corporate Affairs, Regulation, Legal and Compliance departments which provide advice to the Company on the interpretation of political and regulatory change. The Company's regulatory obligations are reported in accordance with the RIGS and Data Assurance license conditions which have a substantial governance regime behind each submission. In addition, there is proactive engagement with regulators, politicians, officials and other stakeholders on these issues.
- **Network Operational Management** – The Company has an obligation to maintain and enhance its network and ensure its resilience. Failure to manage the operational network performance where external factors can affect operability that may result in loss of supply, customer dissatisfaction and regulatory penalties. A robust asset management and quality assurance process is in place to ensure that equipment is of the correct standard and specification to provide a safe, efficient and reliable network now and in the future. The impact of adverse weather on our network infrastructure is an annual event and due to the ongoing impact of global climate change, it is anticipated that the volume and impact of these events will increase. The Company has many years' experience in dealing with these events and there is significant effort directed to forecasting such events and ensuring that there are plans in place to deal with them, both in the control room and in the field. This involves early deployment of staff to potentially affected areas and ensuring sufficient staff and other resources are available to effectively deal with any disruption.
- **Cyber Security Resilience** - With the increased incidence of cyber-attacks over recent years there is a risk to the Company's key systems and, as a result, the infrastructure network could be compromised or rendered unavailable. To mitigate this risk, the Group and Company are investing in a long-term security programme including liaising with relevant external stakeholders, maintaining business continuity plans and disaster recovery sites, and ensuring staff awareness of IT security issues and their importance.

Understanding and managing our principal risks *(continued)*

- **Network Asset Management** – The Company continues to manage the ever changing demands placed on network assets. Failure to monitor and understand network asset health conditions could compromise the targeted investment strategy, resulting in a decline of network performance with resulting penalties and reputational damage. It is critical that these projects are delivered on time, on budget and to a high standard given the long-term nature of the business. The Investment Management Framework facilitates for the robust evaluation of every decision based on safety and environment, costs, risks and performance implications over the whole asset lifecycle. Clear roles and responsibilities are established within asset management, the technical design authority and the Electricity Distribution sub-committee which oversees the investment plan. The roll-out of continuous staff training programmes on network data management offers further support.
- **Project Delivery** – The Company continues to deliver its capital investment programme with a number of ongoing network construction and IT projects. It is critical that these projects are delivered on time, on budget and to a high standard given the long-term nature of the business. The Company will typically manage the development process and organise the delivery of the project by third party contractors and suppliers, taking a pro-active oversight role during the procurement and construction phase. Whilst this model ensures that the correct skills are leveraged, there is a risk of supplier failures, faulty components, and quality defects. The Group-wide Large Capital Projects Governance framework helps to mitigate this risk by ensuring a consistent approach to project development and delivery as well as proactive engagement with the supply chain.
- **Customer Safety and Relationship Management –** The Company continues to manage and meet Customer and third party expectations, including Asset Owners, Retail Group and local authorities, in order to prevent customer and stakeholder dissatisfaction and associated reputational and financial loss. The Company mitigates this risk through the work of stakeholder advisory panels, local and community resilience plans and continuous training for customer facing staff. Regional engagement roles and relationships are established within the Company's communities, while a stakeholder mapping and vulnerability tool has been established to support customer requirements.
- **Change Transformation** – The energy industry is undergoing constant technological and regulatory change. It is important that the Company is able to stay at the forefront of the industry by identifying emerging trends and developing strategies to exploit competitive opportunities. Through the RIIO-ED1 settlement and on approach to RIIO-ED2, the Company has proposed significant reductions in the overall cost and improvements in the standard of service that customers can expect to receive. To deliver this successfully, we will need to transform our business and people, delivering major cost efficiencies, new IT systems and improvements in customer service. The Company has in place a RIIO-ED2 blueprint and a Change Delivery Project Team to aid this, while maintaining strong governance processes and procedures at Board and Leadership team levels to monitor the transformation process.
- **People and Culture**- In order to support a strong business culture which meets the demands of the customer focused delivery model, the Company must continue to attract, develop and retain a skilled workforce. In order to mitigate the risk of failing to attract talent, the Company continues to enforce a People Strategy which delivers on highlighting the value in attracting an inclusive and diverse workforce. Through the Networks People Sub Committee and its continuous management of talent and execution of an effective recruitment strategy, the operating model will continue to achieve high performance whilst maintaining an inclusive culture.
- **Sustainability** - The Company continues to transition the network to a flexible system which can accommodate international and government net zero carbon economy goals. Ambitious targets in respect of electric vehicles and smarter electricity systems usage inevitably increase expectations of investors and stakeholders. The Company business strategy remains firm and has hardwired the transition to net zero to its core, building the assets, infrastructure and services to help achieve decarbonisation. The Distribution Executive Committee continues to work to identify, quantify and articulate social and environmental impacts in a way that generates value for society whilst ensuring the network does not fail to achieve the targets set.

Coronavirus

The coronavirus pandemic continues to impact business in the UK and Ireland and has resulted in the Distribution Executive Committee undertaking an additional assessment of each of the Principal Risks. Completed by the members assigned to oversight committees, the further assessment required consideration of additional key developments based on information collected from the business and re-assessing the risk trends to reflect any identified impact from the virus. The overall conclusion of this assessment was that the human, social and economic impact of coronavirus has increased the prevalence of a number of the influencing factors detailed against several of the Company's Principal Risks. The impact of Coronavirus on the Company's business continues to offer uncertainty and continuous consideration is offered to specific developments in order to monitor any potential increase in the likelihood of occurrence of the risks and any increase in the materiality of their impacts should they occur.

Section 172(1) Statement

Section 172 of the Companies Act 2006 requires a director of a company to act in the way he or she considers, in good faith, would most likely promote the success of the company for the benefit of its members as a whole. In furtherance of this, section 172 requires a director to have regard amongst other matters, to the:

- likely consequences of any decisions in the long term;
- interests of the company's employees;
- need to foster the company's business relationships with suppliers, customers and others;
- impact of the company's operations on the community and environment;
- desirability of the company maintaining a reputation for high standards of business conduct; and
- need to act fairly as between members of the company.

In discharging their section 172 duties, the Directors of the Company, have regard to the factors set out above. They also have regard to other factors which they consider relevant to the decision being made. Those factors, for example, include the Company's applicable regulatory and legal obligations.

The Directors acknowledge that every decision taken will not necessarily result in a positive outcome for all of the Company's stakeholders. However, by considering the Company's purpose and values, together with its strategic priorities, and having agreed processes in place for decision-making, they do aim to ensure that decisions are consistent and appropriate in all circumstances. Details of the mechanisms which are in place to assist the Directors in understanding relevant views, including how these have been considered during the year, are set out on pages 9 to 13.

As is normal for large companies, authority for day-to-day management of the Company is delegated to senior management, with the setting and oversight of business strategy and related policies remaining the responsibility of the Directors. The Company's statement on its corporate governance arrangements on page 17 sets out further details of how this is governed within the SSE Group and the Company.

The Company is represented by the Directors on the Distribution Executive Committee which reviews health and safety, financial and operational performance and legal and regulatory compliance at every meeting, in addition to other pertinent areas over the course of the financial year, including:

- the Company's business strategy;
- key risks;
- stakeholder-related matters;
- diversity and inclusion;
- environmental matters;
- corporate responsibility; and
- governance, compliance and legal matters.

This is done through the consideration and discussion of reports which are sent in advance of each meeting and through presentations to the Executive Committee. In accordance with the Company's governance framework, the Board of Directors review the health and safety, financial and operational performance, and legal and regulatory compliance throughout the financial year. Some decisions are reserved matters for the Group Board of Directors as stipulated within the governance framework for the Company.

The strategic and operational priorities of the Company are compared to its long term targets and obligations to shareholders, the regulatory framework for which it is governed by, and the contribution to society. The nature of the Company's principle activity to invest, maintain and operate the electricity network in the north of Scotland which means it actively engages and promotes societal welfare. The investment in electricity distribution assets is to improve network resilience, reduce faults, and improve network reliability for the benefit of society. Additionally, there has been significant investment in the distribution network infrastructure to facilitate the continued drive towards the electrification of transport and heat. This supports the governments net zero emissions targets which benefits society as a whole. The Company continues to advocate for investment in line with the draft RIIO-ED2 business plan.

Section 172(1) Statement *(continued)*

In line with the above, the Distribution Executive Committee, during the financial year, approved several capital investment projects to proceed to full construction as set out in the Company's Financial Authorisation Policy. This included specific projects that required further financial approval by the Company's Board of Directors as well as those that required financial approval by SSE Group Board of Directors. Other strategic projects approved at the executive level include finalisation of the Company's customer based approach to its RIIO-ED2 business plan as well as the Western Isles subsea cable fault upgrade. The Executive Committee also committed to deliver a safe, reliable and efficient approach to subsea cable investment, ensuring optimisation of value for customers by improving the prediction of subsea cable failure events.

Stakeholder engagement

The Company's stakeholders are people, communities and organisations with an interest or concern in its purpose, strategy, operations and actions, and who may be affected by them. This includes: shareholders and debt providers; employees; government and regulators; NGOs (non-governmental organisations), communities and civil society; suppliers, contractors and partners; and customers. The perspectives, insights and opinions of stakeholders are recognised as a key factor in the relevant operational, investment and business decisions taken by the Company and its Directors, to ensure that as a whole they are more robust and sustainable.

While there are cases where the Directors may judge it appropriate to engage directly with certain stakeholder groups, the size and spread of both the Company's stakeholders and those of the Group, of which the Company sits within, means that stakeholder engagement takes place at many different levels. This includes at Group level, business unit level, company level and operational level. This holistic approach avoids operating in isolation and allows a broader representation and deeper understanding of all stakeholder views and contributes towards a greater outcome for business, environmental, social and governance matters.

If the UK is to fully decarbonise the economy by 2050, this will require both a significant increase in electricity demand and a fundamental shift in the way it is consumed as millions more electric vehicles, hundreds of thousands of heat pumps and embedded generation and storage come onto the system in the coming years. That means the Company's distribution network has a critical role to play and the next RIIO-ED2 price control period between 2023 and 2028, is key to unlocking the strategic, anticipatory investment required to deliver the resilience, flexibility and responsiveness required.

The Company has consulted extensively with all stakeholders to build a robust and compelling business plan and there is excitement about the role the Company can play in the transformation journey that lies ahead.

The Company continues to adapt and seek improved engagement opportunities with customers, suppliers and other key stakeholders. In doing so, the Company also adheres to the Group's wider stakeholder engagement strategy. For more information regarding the Group's approach to stakeholder engagement, please see the 2020/21 Annual Report available at www.sse.com.

Employees

The Group and the Company's strategy includes being a great place to work; providing an inclusive, fulfilling and high-performing workplace. This means maintaining a healthy business culture; adopting a responsible approach to employee relations; providing good employee benefits; and enabling people to develop their careers.

From March 2020, the Group and Company's immediate safety and health priority was the management of the coronavirus crisis and associated risks. This demonstrated why a robust health and safety culture is so important, with the Company able to build on existing approaches to ensure it took care of employees and was able to implement quickly new measures and provide new guidance.

The Group and Company has emphasised the importance of parity of focus between mental and physical health, with initiatives including Mental Health First Aiders, employee assistance counselling, partnership counselling with Nuffield Health, and access to a range of wellbeing programmes, as well as muscular-skeletal treatments and a range of subsidised and participatory physical exercise programmes.

Stakeholder engagement *(continued)*

Employees (continued)

In response to the potential increase in stress levels and isolation as a result of the majority of employees working from home on a full-time basis, new initiatives were also introduced during 2020/21 for employees. This includes online workout sessions, online learning with topics ranging from mental health to resilience and coping with change, mindfulness conference calls and weekly virtual wellbeing cafes.

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

Rewarding employee contribution

Employees at all levels within the Group are measured against the same framework, and the formal bi-annual performance review sessions are designed to feedback to employees on their performance as well as provide structured career conversations which encourage employees to think about their opportunities for personal and professional development. The Group's well-established approach to performance management has a structured framework which assesses employee performance against individual agreed objectives as well as alignment to the core values of Safety, Service, Efficiency, Sustainability, Excellence and Teamwork.

The Group offers a wide range of employee benefits. As well as contractual benefits determined by factors such as seniority and length of service, including a company car/allowance and private medical insurance, the Group offers a comprehensive suite of non-contractual voluntary benefits to all employees. The Company also offers all-employee flexible working arrangements, share plans, health benefits, gym membership, childcare vouchers, a holiday purchase scheme and technology loans. The Group has recently rolled out CarPlus, a new salary sacrifice car scheme open to all employees.

The Group's maternity benefits are market-leading with 21 weeks leave at full-pay and gradual return to work policy which offers those returning from maternity leave the opportunity to work 80% of their contractual hours but still receive full pay and benefits for up to six months.

Employee participation

The Group's long-established teamwork value has been an enduring value that guides employees in their day-to-day working lives.

Each year the Group runs an employee engagement survey to better understand the level of employee engagement, however these were run more regularly during the coronavirus crisis period to capture employee sentiment on a number of key themes, including communication, strategy, leadership and wellbeing. This feedback has influenced employee focused decisions on ways of working, communication and wellbeing. SSE's September 2020 employee engagement survey had a participation rate of 82% and an engagement score of 82%. This was 3% above the utilities sector benchmark and 8% above the UK benchmark.

Over the past year, SSE has enhanced its employee voice strategy with the addition of exit surveys. The exit survey aligns to SSE's overall approach to gathering employee engagement insights through its employee engagement survey, and therefore allows a comparison of top/bottom scoring answers for ex-employee sentiment on the company. The results are enabling SSE to gather meaningful and robust insights into why people leave the company, informing actions which aim to improve the employee experience. Details of these actions including the Group's support for customers, employees, suppliers and communities can be found at www.sse.com.

The views of Company employees, as gathered through the Group survey, are reviewed at business unit level by the Executive Committee. This data is supplemented by monthly KPIs, tailored business unit led engagement and the work of the Group's dedicated non-Executive Director for Employee Engagement, who provides feedback to the Managing Director of each business unit following relevant engagement. The Company also undertakes a standalone engagement survey for employees which performed well and for which there is a clear time-bound action plan to delivery improvements in employee engagement. People strategies and action plans to address employee views are developed and overseen by the business unit Executive Committee/the Directors in response to feedback received.

Stakeholder engagement *(continued)*

Customers

The Company has a well-established customer engagement channel to ensure the perspectives of all customers are considered. A significant part of the Company's engagement with the government and the regulator relates to the maintenance and development of reliable and sustainable electricity networks for the benefit of customers, whilst also delivering value for money. Material considerations include assurances over affordable and accessible energy, providing a quality customer service as well as the responsiveness to vulnerable customers in need.

The coronavirus pandemic has demonstrated the complex and transient nature of consumer vulnerability. Significant financial challenges have been brought to many of the Company's customers and it has shown how important it is to remain flexible, agile and continually evolve to meet customers' needs.

The Company serves over 0.7m customers and adapted its service provision quickly to support customers in 2020/21. The Company's industry-leading customer vulnerability mapping tool was enhanced in 2020/21 with the addition of a new social indicator showing levels of Universal Credit uptake to complement existing data on low income and long-term unemployment. The mapping tool was shared widely with partners to inform and support more accurate coronavirus responses.

The Company's partnerships to support vulnerable customers helped thousands of households in 2020/21 as the Company extended its energy advisor programme with Citizens Advice Scotland for another 12 months and enhanced the partnership with NHS Home and Well partnership to specifically target support for people coming out of hospital.

The Company also launched a new joint Priority Services Register (PSR) Scotland website in collaboration with Scottish Water and SP Energy Networks to offer a PSR one-stop-shop across Scotland, making it easier for partners to promote and customers to sign up. This supplemented a continued focus on energy efficiency, with the trebling of referrals from the Company to energy efficiency agencies in Scotland.

The Company's comprehensive engagement has shaped the direction of the Company's draft RIIO-ED2 business plan submission. The Directors continue to monitor overall business direction and customer performance to ensure delivery of an appropriate level of service and investment.

Suppliers, contractors and partners

The Company continues to work closely with suppliers to ensure its values on issues such as environmental protection, safety and modern slavery are upheld throughout its supply chain. The Company facilitates value-adding conversations on subjects like innovation and future growth whilst ensuring relationships are maintained at all levels, from project teams on the front line through to senior management and Directors. To ensure high operational standards, onsite training is held for contractors and quality and health and safety audits are undertaken by the Group. This includes the Group's in-year development of a new Sustainable Procurement Code and linked Supplier Guidance document which aligns to those UN Sustainable Development Goals material to the Company and Group's business. Material considerations include assurances that social and environmental impacts are managed and mitigated, as well as ensuring innovation relating to the project design and delivery supports the Company in the drive to net-zero transition. Improved engagement with suppliers is demonstrated by major project updates which during 2020/21 include progress on the electrification of the UK's ambitious Electric Vehicle targets with the Company publishing its strategy in March 2020.

In order to ensure that there has been adequate engagement in fostering the Company's business relationships with suppliers, customers and other relevant parties' representations are made on a regular basis at business unit level by business partners which represent the areas of Procurement, Corporate Affairs and Legal within the Company. Such representations are designed to inform the Directors of the current nature of the relationship, the strategic significance that the relationship offers to support the objectives of the business and the prospects or issues associated with the continued fostering of the relationship.

Strategic Report *(continued)*

Stakeholder engagement *(continued)*

Government and regulators

During 2020/21, the Company continued to extensively liaise with regulatory officials and responded to all material regulatory consultations, with dedicated teams working to communicate business strategy and investment decisions. The Company continues to take an active role in the development of regulations and policies which impact upon the Company and its customers.

As part of RIIO-ED2, which sets out the price control from April 2023, the Company engaged extensively with stakeholders to co-create the draft business plan submission. The Directors continue to monitor engagement activity and responses to regulators to ensure that strategic, financial, investment and operating frameworks remain aligned to the external landscape.

Communities

The Company's core purpose is to deliver a safe, reliable and accessible service to the customers and the communities it serves, putting the needs of all consumers at the centre of its activities. This year has been unlike any other and the Company has been working hard to support the most vulnerable in society which has been more critical than ever. Great strides have been made to increase fuel poverty support, implementing a two-tiered targeted approach to engage harder to reach communities.

Mental health support has been also been prioritised as many may have been affected by the pandemic. Customer facing employees have received refreshed training in this area to ensure they are well equipped to support our customers.

The Company takes a proactive approach to engaging with communities in the pursuit of environmental protection and decarbonisation. A variety of platforms are used to communicate with local community groups and residents to ensure those that are affected are well informed and have the scope to challenge on any concerns. These methods include attendance at community meetings and public information days as well as Company publications.

As an essential service provider, the Company has a vital role to play to tackle social issues and our commitment to addressing those issues relevant to the most vulnerable in society, remains a strong focus to ensure no one is left behind.

Environment

The Company operates a substantial environmental policy in conducting its operations with a clear focus on protecting the natural environment within the north of Scotland.

The climate emergency remains a profound issue for human kind and the Company has hardwired the transition to net zero to its core through continuing to build and maintain infrastructure and services required to help achieve decarbonisation. As a responsible developer, the Company actively continues to identify, quantify and articulate social and environmental impacts with communities across its network areas. During the year, the Company has managed those impacts through the development and application of smarter on-site electricity generation, creating value for society and future generations in the process. The Company also became the first UK Distribution Network Operator to commit publicly to setting science-based targets, in January 2021. The targets can be found in the draft business plan submission for RIIO-ED2.

The next decade will see widespread and permanent change in how we operate and travel, and as a network operator, the Company has a critical role to play in ensuring a successful transition. In particular, the Company's network has a central role in the movement towards decarbonised transport by providing secure, resilient infrastructure which can support the national target of 10 million electric vehicles on UK roads by 2030.

As the low-carbon energy transition develops, the Company continues to deliver sustainable energy investment across the network. The Company provides vital infrastructure which is essential to improving service and reliability for customers. Whilst doing so, the Company works to protect the environment and local wildlife in the vicinity of its infrastructure. A dedicated programme of work has been adopted in order to preserve network efficiency whilst ensuring environmental needs are met.

Environment (*continued*)

More information on the Group's approach to managing our environmental impact, including the recently published 'greenprint' for a cleaner, more resilient recovery from the economic impact of coronavirus is contained in the 2020/21 Annual Report, available at www.sse.com.

Internal control

The Group's Audit Committee performs a review of the effectiveness of the system of internal control annually across the Group. This covers all material controls including financial, operational and compliance controls. When undertaking the review of the effectiveness of the System of Internal Control, 10 key management control areas are considered together with any planned improvements to enhance existing controls. During the year, the Committee stood up a project team to assess the financial reporting control environment in anticipation of a SOX style framework being introduced in the UK. The Committee will continue to monitor regulatory developments and will receive regular updates from the project team. Following the Committee's review and recommendation, the Group Board agreed that the Group's System of Internal Control (including risk management) continues to be effective.

Taking into account the actions taken, the Group Board also confirms that no significant failings or weaknesses have been identified during the year. Processes are in place to ensure that necessary action is taken, and progress is monitored where areas for improvement have been identified.

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

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

Key contractual arrangements

The Directors consider the Service Level Agreement in place between the Company and SSE Services plc for the provision of corporate services to be essential for the continuance of the Company's operations in the short-to-medium term. Due to the fact that it is provided by a fellow subsidiary of the Group, the risk of this contract being terminated is low.

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

Operational resources available

The Company has 1,487 employees which it calls on to maintain its distribution network and carry out investment in future developments. The Company also draws upon Group shared services covering central functions such as finance, HR, regulation, health and safety, company secretarial and insurance services. All such services are provided under an appropriate Service Level Agreement. In addition to these employees, the services of key contractors are called upon in a number of large capital projects to ensure that these projects are delivered on time and on budget.

Capital structure

The Company regards its capital as comprising its equity, cash and borrowings. Its objective in managing capital is to maintain a strong balance sheet and credit rating so as to maintain investor, creditor and market confidence and to sustain future development of the business.

Treasury policy, objectives and financial risk management

The Group's treasury policy is designed to be prudent and flexible. In line with that, cash from operations is first used to finance regulatory and maintenance capital expenditure and then dividend payments, with capital and investment expenditure for growth generally financed by a combination of cash from operations; bank borrowings and bond issuance. In 2020/21 growth was also financed by disposal proceeds.

Exposure to interest rate risk arises in the normal course of the Company's business. Derivative financial instruments are entered into to hedge exposure to risk. The objectives and policies for holding or issuing financial instruments and similar contracts, and the strategies for achieving those objectives that have been followed during the year are explained in note 22.

The Company's financial risk is managed as part of the wider Group risk management policy. For more information regarding the Group's approach to financial risk management, please see the 2020/21 Annual Report available at www.sse.com.

Liquidity, borrowings and financial resources available

The Group's Treasury function acts on behalf of the Company and is responsible for managing the banking and liquidity requirements of the Group, risk management relating to interest rate and foreign exchange exposures and managing the credit risk relating to the banking counterparties with which it transacts. Short term liquidity is reviewed daily by Treasury, while the longer term liquidity position is reviewed on a regular basis by the Board. The department's operations are governed by policies determined by the Board and any breaches of these policies are reported to the Tax and Treasury Committee and Audit Committee.

As part of the Group, the Company has significant resources which it can draw upon to meet its service commitments. The Company benefits from Group-wide treasury management functions in order to provide adequate financing, with a cash balance of £1.6bn at 31 March 2021 and undrawn facilities totalling £1.5bn available to the Group at 31 March 2021 which could be made available to the Company if required. These facilities are a £1.3bn revolving credit facility with a March 2026 maturity and a £200m bilateral facility with an October 2025 maturity and an option to extend for a further year to October 2026. As at 31 March 2021, both facilities were undrawn.

The Company has loans of £797.6m *(2020: £696.2m)* of which £650.0m *(2020: £550.0m)* is due to other Group companies. Of the total, interest is paid at fixed rates on £650.0m *(2020: £550.0m).* The remaining loan amounts to £147.6m *(2020: £146.2m)* and is an index-linked bond.

As at 31 March 2021, the weighted average interest rate payable was 3.57% *(2020: 3.74%)* and the weighted average remaining term was 13.07 years *(2020: 13.71 years*).

Taxation

The headline effective tax rate, which includes the impact of substantively enacted changes in the UK corporation tax rate, is 18.7% compared with 30.7% in the previous year. The prior year rate of 30.7% was a result of a deferred tax charge of £8.3m to reflect the amendment to the main rate of corporation tax from 17% to 19% which became effective in the year.

Dividend

The Directors did not declare a dividend for the year ending 31 March 2021 *(2020: £85.0m).*

Strategic Report *(continued)*

Pensions

8% *(2020: 9%)* of employees of the Company are members of the Scottish Hydro Electric Pension Scheme, which, at 31 March 2021 on an IAS 19 basis had a surplus, net of deferred tax, of £439.9m included in the Group Financial Statements *(2020: £432.7m).*

On behalf of the board

Gregor Alexander (Jul 23, 2021 14:25 GMT+1)

Gregor Alexander
Director
23 July 2021

Scottish Hydro Electric Power Distribution plc

Corporate Governance Statement

As a subsidiary company of the Group, the corporate governance arrangements which apply to the Company are defined by SSE's Group Governance Framework. This is set out on pages 102 and 103 of the SSE plc Annual Report, with the Company being part of the SSEN Distribution business unit.

The Group Governance Framework is reflective of the Principles and Provisions of the UK Corporate Governance Code (the Code) which apply to the parent company, SSE plc. It defines the delegation of authority and accountability within the Group, enables review and challenge of management performance, is a pillar of SSE's System of Internal Control, and supports the processes by which principal and emerging risks are identified and managed. The Directors of the Company discharge their duties in line with the governance standards and processes agreed at Group level.

The Company itself does not have listed shares and therefore is not subject to the Code. It has not voluntarily applied the Code nor another publicly available corporate governance code and has instead operated within the Group Governance Framework described above and below.

The Group's approach to corporate governance and compliance with the Code can be found in the Directors' Report within the SSE plc Annual Report and Accounts 2021 at www.sse.com/reportsandresults.

SSE plc Group ("the Group")

The Group's core purpose is to provide the energy needed today while building a better world of energy for tomorrow. Its vision is to be a leading energy company in a net-zero world and its strategy is to create value for shareholders and society in a sustainable way through successful development, efficient operation and responsible ownership of energy infrastructure and businesses. All of which are underpinned by the SSE SET of core values: Safety, Service, Efficiency, Sustainability, Excellence and Teamwork; that are designed to guide decisions and actions within SSE and contribute to the overall culture.

The above matters are reserved for, and set by, the Group Board, who ensures that purpose, strategy, values and culture are aligned. Subsequent implementation is a responsibility of the SSE Group Executive Committee. Each business unit, and in turn, subsidiary Company and its Directors, is further accountable to executive management and ultimately the Group Board, for executing supporting business strategies within agreed Group parameters and promoting the desired culture. The Directors therefore set the strategic aims of the Company, supervise management, monitor and report on performance, approve investment within delegated levels and are responsible for all statutory and regulatory approvals. These responsibilities are set out in agreed Terms of Reference.

More on the Company's strategy and business objectives can be found from page 2 of the Strategic Report.

More on SSE's purpose and strategy can be found on page 8 to 9 of the SSE plc Annual Report and more on culture can be found on page 112.

There are five principal Board committees; a Nomination Committee, an Audit Committee, a Safety, Health and Environment Advisory Committee, an Energy Markets Risk Committee and a Remuneration Committee. Full details of the role of each Committee, membership and work undertaken during 2020/21 is set out in the published annual report of the Group, which is available at www.sse.com.

Richard Gillingwater stepped down from the Board and role of Chair on 31 March 2021 and Crawford Gillies stepped down as non-Executive Director and Senior Independent Director on 30 September 2020. The Board approved the appointment of Sir John Manzoni as Chair from April 2021 and as announced in March 2020, Dame Angela Strank joined the Board of SSE plc as a new independent non-Executive Director on 1 May 2020. The Board now comprises the Chairman, three Executive Directors, a Senior Independent Director and five independent non-Executive Directors. This gives the Board a good balance of independence and experience, ensuring that no one individual or group of individuals has undue influence over the Board's decision making.

Scottish Hydro Electric Power Distribution plc

Corporate Governance Statement *(continued)*

Scottish Hydro Electric Power Distribution plc (“The Company”)

The following comments on the arrangements for the Company.

Board of Directors

During the year the Board comprised seven Executive Directors and five Non-Executive Directors, one of whom is the Chair of the Board, an Executive Director of the Group and member of the Group Executive Committee. None of the Directors are Directors of Group Companies involved in Retail or Wholesale activities. Two of the Non-Executive Directors on the Board during the course of the financial year were Sufficiently Independent Non-Executive Directors as required under the terms of Standard Condition 43A of the Company’s regulatory licence. As the Company is a wholly owned operating subsidiary within the SSE Group, the Directors believe that the Board is of an appropriate size in the context of the overall Group Governance Framework.

The Executive Directors are experienced senior business leaders and are deemed to possess the appropriate breadth of knowledge and expertise to discharge their role effectively. The Non-Executive Directors provide an appropriate degree of independent judgement and challenge to ensure balanced and fair decision-making and outcomes. The operation and effectiveness of the Board is the ultimate responsibility of the Chair, who is supported in their role by the Company Secretary. Agreed procedures are in place to manage and mitigate actual or potential conflicts of interest with Board or Company business.

The Board does not have a supporting Nomination, Remuneration or Audit Committee. These functions are dealt with, where required, in conjunction with the relevant committee of the Group Board.

SSE has a Group-wide inclusion and diversity strategy including self-led gender ambitions, details of which can be found on pages 49 and 50 of the SSE plc Annual Report. Any changes and appointments to the Board consider both SSE’s approach to inclusion and diversity and the desire to have a Board which is balanced overall and supports the Company’s needs.

Director	**Attendance**
Gregor Alexander (Non-Executive Director) (Chairman)	8 of 8
Colin Nicol (Resigned 04/01/21)	4 of 5 (to date of resignation)
Rob McDonald	8 of 8
Chris Burchell (Appointed 04/01/21)	3 of 3 (since appointment)
Eliane Algaard (Appointed 01/09/20)	6 of 6 (since appointment)
Mark Rough (Appointed 01/04/20)	7 of 8
Sandy Mactaggart (Appointed 23/02/21)	2 of 2 (since appointment)
Maz Alkirwi (Appointed 23/02/21)	2 of 2 (since appointment)
Rachel McEwen (Non-Executive Director)	8 of 8
Katherine Marshall (Non-Executive Director)	8 of 8
David Rutherford (Independent Non-Executive Director)	8 of 8
Gary Steel (Independent Non-Executive Director)	8 of 8

Board effectiveness

On appointment all Directors receive induction to the Board and briefings on areas pertinent to their role such as a Director’s legal duties. The ongoing effectiveness of the Board is supported by performance evaluation and a commitment to personal development and training by each Director.

Regular Board evaluation is facilitated by the Company Secretary, through which the Director’s reflect upon, and agree, areas for improvement based on an objective assessment of the Board’s operations. Following such assessments, actions are implemented and tracked in advance of further performance evaluations in 2021/22.

Scottish Hydro Electric Power Distribution plc

Corporate Governance Statement *(continued)*

Opportunity, Risk and Internal Control

The long-term sustainable success of the Company, including the opportunities and risks to this, are explicitly considered by the Directors and within strategic decision making. Further details can be found throughout the Strategic Report.

Remuneration

The Remuneration of the Director's is set in line with overall SSE Group policy and further information can be found in note 5.

Stakeholder relationships and engagement

Details of the Company's stakeholders and the associated engagement which takes place can be found from page 9 of the Strategic Report.

Going Concern

The Directors assess that the Financial Statements should be prepared on a going concern basis. In making their assessment, the Directors have considered future cash flows, including sensitivities on future cashflow projections resulting from the coronavirus pandemic, and the level of headroom on long-term loans and bonds for the period to 31 December 2022.

In making this assessment, the Directors have considered the impact of a number of severe but plausible scenarios as identified by the Business Unit Executive Committee. These are detailed within the Principal Risks outlined in the Company's Strategic Report. As it is highly unlikely that all scenarios could or would manifest in any single financial year, the Directors have considered an extreme combination which assumes that the "Network Resilience and Integrity", "Safety, Health and Environment" and "Cyber Security" risks manifest in the same year – these being the Principal Risks with the greatest financial impacts.

Additional cash flow modelling, including the impact of periods of reduced demand and stressed conditions on the Company's ability to refinance maturing debt, was carried out against which operational and financial mitigants were also considered. This cash flow modelling displays the potential prospective impact on the financial position of the Company for the foreseeable future, based on plausible downside scenarios which may materialise over the coming period.

As part of the stress testing performed, the Directors have considered future cash flows, including the above-named sensitivities on future cashflow projections resulting from the coronavirus pandemic, and the level of headroom on long-term loans and bonds. The Directors believe that on considering the impacts of the coronavirus pandemic, it is reasonable to assume that access to available Group financing will continue, whilst the significance of the Company's main revenue streams would indicate that a modest drop in revenue could be feasibly determined to have a limited impact on the overall operations of the Company.

The Group have provided a letter of support confirming it can provide support for a period of 12 months from the date of signing of these accounts if required. The Directors are satisfied that the Group has the ability to provide this support, if required. In reaching this conclusion they considered the resources that the Group has in place and available to it and their forecast business plans amidst the current pandemic. For more information regarding the Group's going concern status, please see page 263 of the 2020/21 Annual Report available at www.sse.com.

Through consideration of these scenarios, together with the receipt of a Letter of support received from the Group, the Directors are satisfied that the Financial Statements are prepared on a going concern basis.

Viability Statement

The Board has voluntarily carried out an assessment of the longer-term viability of the Company consistent with the assessment and governance approach undertaken at Group level by SSE plc.

In doing so, the Board has assessed the prospects of the Company over the next 3 financial years to 31 March 2024. The Directors have determined that as this time horizon aligns with the Company's capital programme and is within the strategy planning period, a greater degree of confidence over the forecasting assumptions modelled can be established.

This statement is included solely for information.

In making this statement the Directors have considered the resilience of the Company taking into account its current position, the impacts of the coronavirus outbreak, the Principal Risks it faces and the control measures in place to mitigate each of them. In particular, the Directors recognise the significance of the Company's regulated revenue stream, strong balance sheet and access to available resources including the SSE Group's undrawn committed lending facilities of £1.5bn.

To support this statement, over the course of the year a suite of severe but plausible scenarios has been developed for each of the Principal Risks facing the Company and stress testing has been undertaken against available forecast financial headroom. Examples include critical network failure (for Network Operational Management), and impact of a cyber-attack to our IT network (for Cyber Security Resilience). Consideration of the coronavirus pandemic has also been considered within the scenario analysis.

Upon the basis of the analysis undertaken, and on the assumption that the fundamental regulatory and statutory framework in which the Company operates does not substantively change, the Directors have a reasonable expectation that the Company will be able to continue to meet its liabilities as they fall due in the period to 31st March 2024.

Scottish Hydro Electric Power Distribution plc

Directors' Report

The Directors present their report together with the audited Financial Statements for the year ended 31 March 2021.

Reporting requirements on the Company's principal activities and future developments, its principal risks and uncertainties and its key performance can be found in the Strategic Report.

1 Principal activities

The Company is responsible for managing an electricity distribution network, serving around 740,000 customers in the north of Scotland. Distribution of electricity and the level of capital investment within the network area is a monopoly activity and is closely regulated by Ofgem within a framework known as the Price Control. The Company also carries out the business of provision of new electrical connections services within its licensed area and the construction and management of out-of-area electricity networks in Scotland. A full review of the year is contained within the Strategic Report section of these Financial Statements.

2 Results and Dividends

The profit for the financial year amounted to £57.4m *(2020: £44.8m).* The Directors did not declare a dividend in the year *(2020: £85.0m)*.

3 Directors

The Directors and Secretary who served during the year are listed on page 1. In accordance with the Articles of Association of the Company the Directors are not required to retire by rotation.

4 Indemnification of Directors and insurance

The Directors have the benefit of an indemnity provision contained in the Company's Articles of Association. In addition, the Directors have been granted a qualifying third-party indemnity provision which was in force throughout the financial year and remains in force. Also, throughout the financial year, the Company purchased and maintained Directors' and Officers' liability insurance in respect of itself and for its Directors and Officers.

5 Political donations and expenditure

The Company operates on a politically neutral basis and does not make any donations to political parties, political organisations or independent election candidates. During the year, no political expenditure was incurred and no political donations were made by the Company.

6 Corporate governance

The Corporate Governance Statement for the Company is outlined on page 17.

7 Accounting policies, financial instruments and risk

Details of the Company's policies with regard to financial instruments and risk, are provided in Note 22 to the Financial Statements.

8 Research and development

The Company is involved in a range of innovative projects and programmes which are designed to progressively transform the energy system. A number of these projects and programmes are referred to in the Strategic Report in pages 2 to 16.

9 Employment of disabled people

The Company has a range of employment policies which are designed to ensure that everyone, including those with existing or new disabilities and people of all backgrounds, are dealt with in an inclusive and fair way from the recruiting process on through their career, whether that means access to appropriate training, development opportunities or job progression. The Group and Company have a range of employment policies which clearly detail the standards, processes, expectations and responsibilities of its people and the organisation.

10 Auditor

Each of the Directors who held office at the date of approval of this Directors' Report confirms that, so far as each Director is aware, there is no relevant audit information of which the Company's Auditors are unaware and each Director has taken all the steps that ought to have been taken in his or her duty as a Director to make himself or herself aware of any relevant audit information and to establish that the Company's Auditors are aware of that information.

On behalf of the Board:

Mark McLaughlin (Jul 23, 2021 11:07 GMT+1)

Mark McLaughlin
Company Secretary
23 July 2021

Scottish Hydro Electric Power Distribution plc

Statement of Directors' responsibilities in respect of the Strategic Report, the Directors' Report and the Financial Statements

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law they have elected to prepare the Financial Statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including 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 its profit or loss for that period. In preparing the Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the Financial Statements;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its Financial Statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of Financial Statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

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

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

We confirm that to the best of our knowledge:

- the Financial Statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company; and
- the Strategic Report/Directors' Report includes a fair review of the development and performance of the business and the position of the issuer, together with a description of the principal risks and uncertainties that they face.

We consider the Annual report and Financial Statements to be fair, balanced and understandable and provides the information necessary for users to assess the Company's position and performance.

On behalf of the Board:

Gregor Alexander (Jul 23, 2021 14:25 GMT+1)

Gregor Alexander
Director
23 July 2021

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

Opinion

We have audited the financial statements of Scottish Hydro Electric Power Distribution plc for the year ended 31 March 2021 which comprise the Profit and Loss Account, Balance Sheet, Statement of Changes in Equity and Cash Flow Statement and the related notes 1 to 27, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 101 "Reduced Disclosure Framework (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

- give a true and fair view of the Company's affairs as at 31 March 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

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

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. In our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting:

- We confirmed our understanding of management's Going Concern process;
- We obtained board approved cashflow forecasts for the company and sensitivities prepared by management to 31 December 2022. We tested the arithmetical accuracy of the models and performed reverse stress testing to understand how plausible the severe downside scenarios would need to be to result in negative liquidity;
- We understood that management have assumed that access to Group financing will continue the Going Concern period and we obtained a letter of support from SSE plc confirming this;
- We have considered the ability of the company to rely on parent company support; and
- We considered whether management's disclosures in the financial statements sufficiently and appropriately reflect the going concern assessment and outcomes.

In considering the ability of the company to rely on the parent company support, the following procedures were performed over the group and parent company's going concern assessment:

- We confirmed that the cash flow forecasts prepared by management were consistent with those considered in the Group Going Concern model;
- We confirmed our understanding of group management's Going Concern process as well as the review controls in place over the preparation of the group's Going Concern model and the memoranda on going concern;
- We confirmed that all expected risks to going concern were included within management's going concern assessment;
- We obtained group management's board approved forecast cash flows, covenant forecasts and sensitivities prepared by management to 31 December 2022. We tested for arithmetical accuracy of the models as well as checking the net debt position at the year-end date which is the starting point for the model;
- We assessed the reasonableness of the cashflow forecast by analysing group management's historical forecasting accuracy and understanding how any anticipated continued impact of COVID-19 had been modelled;

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

- We performed reverse stress testing on group management’s forecasts to understand how plausible the severe downside scenarios would need be to result in negative liquidity or a covenant breach. The EY assessment reflects all maturing debt through to 31 March 2023;
- We reviewed group management’s assessment of mitigating options potentially available to the company to reduce cash flow spend in the Going Concern period, to determine their plausibility and whether such actions could be implemented by management. We have obtained analysis to determine whether these were within the control of management and evaluated the impact of these mitigations in light of our understanding of the business and its cost structures;
- We performed a detailed review of borrowing facilities to assess their continued availability to the company and to ensure completeness of covenants identified by group management; and
- We reviewed market data for indicators of contradictory evidence to challenge the Going Concern assessment, including review of profit warnings within the sector and review of industry analyst reports.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company’s ability to continue as a going concern for a period to 31 December 2022.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company’s ability to continue as a going concern.

Overview of our audit approach

Key audit matters	• Carrying value of PP&E, specifically risks around incorrect cost capitalisation • Management override of controls, specifically around revenue recognition
Materiality	• Overall materiality of £3.5m which represents 5% of Profit before tax.

An overview of the scope of our audit

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the company. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the company and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed. All audit work was performed directly by the audit engagement team.

Key audit matters

Key audit matters are those matters that, in our professional judgment, 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 our opinion thereon, and we do not provide a separate opinion on these matters.

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

Key audit matters *(continued)*

Risk	Our response to the risk	Key observations communicated to those charged with governance
Carrying value of PP&E specifically the risk around incorrect cost capitalisation (PP&E NBV 2021: £1.420bn, PP&E NBV 2020: £1.343bn) *Refer to Accounting policies (page 37); and Note 10 of the Financial Statements (page 43)* The PP&E balance in Scottish Hydro Electric Power Distribution plc is quantitatively the most significant. The capitalisation of costs involves a level of judgement and therefore there is a heightened risk of material misstatement in this area. This risk is specifically related to the potential for incorrect capitalisation of costs. The risk is that costs are capitalised that are not capital in nature. Incorrect cost capitalisation could have a significant effect on the carrying value of the Company's Network assets on the balance sheet. This could result in overstated assets and income in the year. It is deemed there is a sufficiently high likelihood of misstatement for this to be classified as a key audit matter.	To respond to the risk, we obtained an understanding of the key controls and processes in place over the capitalisation of costs. We tested selected IT application and manual controls relating to the cost capitalisation process. The following procedures were performed: *Controls Testing* We have tested controls over the authorisation, monitoring and review of capital expenditure in the business. *Additions Testing* We selected a sample of PP&E additions in the year and agreed the details to third party evidence to confirm: - The correct amount was capitalised - The cost was capital in nature in line with accounting standards - Assessed and agreed the appropriateness of overheads capitalised *Journal Entry Testing* We performed a search within our journal entries testing, which included the full population of journals posted in the year, for any manual debit journals posted to fixed assets to identify non-standard additions. For any journals identified we agreed to supporting invoices in line with our fixed asset additions testing approach. *Board Minutes Review* We read Board Minutes to identify any unusual or challenging projects that were receiving executive level attention and cross checked this to our additions work to corroborate our findings. *Disclosure Review* We assessed the appropriateness and adequacy of the disclosures in line with relevant accounting standards. All audit work in relation to this key audit matter was undertaken by the Scottish Hydro Electric Power Distribution plc audit engagement team.	We conclude that the costs capitalised in the year were materially correct as a result of the procedures we performed. We are satisfied with the adequacy of disclosure included in the financial statements.

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

Risk	Our response to the risk	Key observations communicated to those charged with governance
Management override of controls, specifically around revenue recognition (Revenue 2021: £343.2m, Revenue 2020:336.2m) *Refer to Accounting policies (page 36); and Note 2 of the Financial Statements (page 39)* Revenue earned by Scottish Hydro Electric Power Distribution plc mostly relates to billing suppliers for the use of their Networks and new connections to the Network. Revenue recognition is a particular area of focus for our audit. We consider possible areas of management bias and fraud, arising from management override of controls. There is management incentive to post manual credits to revenue to improve Company profitability. There are also instances of manual adjustments to revenue figures, and the accuracy and recording of any such material adjustments may represent a fraud risk of material misstatement to revenue.	To respond to the risk, we obtained an understanding of the key controls and processes in place over revenue recognition and the recording of manual journal entries. We tested selected key IT general controls and performed data analytics procedures. We utilised data analytics techniques to correlate sales through to debtors and subsequently cash. We tested any non-correlating entries to third party evidence to ensure these had been correctly recognised. We also tested a sample of revenue transactions to bank statements to confirm cash receipts. We performed revenue cut-off testing by selecting a sample of transactions pre and post year end and inspecting supporting documentation to verify the period the transaction related to. As part of our journal entries testing, we used risk-based filters to test material manual journal entries made to revenue through to supporting third party evidence, to confirm that this revenue recognition was appropriate and had an appropriate business rationale. *Disclosure Review* We assessed the appropriateness and adequacy of the disclosures in line with relevant accounting standards. All audit work in relation to this key audit matter was undertaken by the Scottish Hydro Electric Power Distribution plc audit engagement team.	We conclude that revenue recognised in the period is materially correct based on the procedures performed. We are satisfied with the adequacy of disclosure included in the financial statements.

In the prior year, our auditor's report included the following key audit matters:

- Carrying value of PPE, specifically the risk around incorrect historical depreciation charges - in the prior year, we identified an error relating to historical depreciation charges. This KAM is no longer relevant given management corrected this error and have implemented system changes to prevent it reoccurring.
- Impact of Covid-19, including going concern assessment – we have removed this as a KAM in the current year as a result of the continued resilience of Scottish Hydro Electric Power Distribution plc. Additionally, in line with ISA (UK) 570 revisions, we are now required to disclose going concern separately in our auditor's report, set out on page 24.
- First year audit transition - This is the second year of auditing the entity and therefore the first year audit transition KAM has been removed.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the company to be £3.5 million (2020: £3.3 million), which is 5% (2020: 5%) of profit before tax. We believe that profit before tax provides us with a consistent measure of underlying year-on-year performance.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the company's overall control environment, our judgement was that performance materiality was 75% (2020: 75%) of our planning materiality, namely £2.6m (2020: £2.4m). We have set performance materiality at this percentage due to our assessment of the control environment of the entity including the attitude and integrity of management and those charged with governance.

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with those charged with governance that we would report to them all uncorrected audit differences in excess of £0.13m (2020: £0.18m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

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

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

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

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

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

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

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

Matters on which we are required to report by exception

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 material misstatements in the strategic report or directors' report.

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

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

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 23, 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.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the company and determined that the most significant are those that relate to the reporting framework (FRS101, Companies Act 2006 and UK Corporate Governance Code) and relevant tax compliance regulations in the UK. We also determined there was no non-compliance with regulatory requirements.
- We understood how Scottish Hydro Electric Power Distribution plc is complying with those frameworks by making enquiries of management and those responsible for legal and compliance procedures. We confirmed our enquiries through our review of board minutes, regulatory correspondence and papers provided to the SSE plc Audit Committee. We assessed the susceptibility of the company's financial statements to material misstatement, including how fraud might occur by meeting with management to understand where they considered there was susceptibility to fraud. We also considered performance targets and their propensity to influence on efforts made by management to manage earnings. We considered the programmes and controls that the company has established to address risks identified, or that otherwise prevent, deter and detect fraud; and how senior management monitors those programmes and controls at a group level. Where the risk was considered to be higher, we performed audit procedures to address the identified fraud risk, management override of controls, specifically around revenue recognition.

Independent Auditor's Report to the Members of Scottish Hydro Electric Power Distribution plc *(continued)*

- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved: journal entry testing, with a focus on manual journals and journals indicating large or unusual transactions based on our understanding of the business and enquiries of legal counsel and management. In addition, we completed procedures to conclude on the compliance of the disclosures in the financial statements and accounts with all applicable requirements.
- We understood the relationship between Scottish Hydro Electric Power Distribution plc and its regulator, the Office of Gas and Electricity Markets (OFGEM), to understand their scope of authorisation and controls the entity has in place to meet their requirements. We requested copies of any correspondence with the regulator that is relevant to our audit and discussed ongoing regulatory matters with the directors.

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

Other matters we are required to address

- Following the recommendation from the SSE plc audit committee we were appointed by the company on 18 July 2019 to audit the financial statements for the year ending 31 March 2020 and subsequent financial periods.
- The period of total uninterrupted engagement including previous renewals and reappointments is 2 years, covering the years ending 31 March 2020 to 31 March 2021.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the company and we remain independent of the company in conducting the audit.
- The audit opinion is consistent with the additional report to those charged with governance.

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.

Ernst & Young LLP.

Nicola McIntyre (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Glasgow
23 July 2021

Scottish Hydro Electric Power Distribution plc

Profit and Loss Account
for the year ended 31 March 2021

	Note	2021 £m	2020 £m
Revenue	**2**	**342.4**	336.2
Other Income		**0.8**	-
Cost of sales		**(66.8)**	(65.8)
Gross profit		**276.4**	270.4
Distribution costs		**(158.0)**	(148.8)
Administrative costs		**(14.9)**	(14.4)
Loss on disposal of property, plant and equipment		**(4.7)**	(5.5)
Exceptional restructuring costs		**-**	(1.7)
Operating profit	**3**	**98.8**	100.0
Interest receivable and similar income	**6**	**3.3**	-
Interest payable and similar charges	**7**	**(31.5)**	(35.4)
Profit before taxation		**70.6**	64.6
Tax on profit	**8**	**(13.2)**	(19.8)
Profit for the financial year		**57.4**	44.8

Continuing operations

The above results are derived from continuing activities.

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

Total other comprehensive income

The Company had no other comprehensive income in the current or prior financial years.

Scottish Hydro Electric Power Distribution plc

Balance Sheet
as at 31 March 2021

	Note	2021 £m	2020 £m
Non-current assets			
Property, plant and equipment	10	**1,420.0**	1,343.6
Intangible assets	11	**30.8**	28.6
		1,450.8	1,372.2
Current assets			
Stocks	12	**2.3**	2.6
Debtors	13	**97.9**	71.4
Restricted Cash	14	**13.4**	-
Derivative financial assets	22	**1.3**	-
Total current assets		**114.9**	74.0
Current liabilities			
Creditors: amounts falling due within one year	15	**(449.9)**	(118.6)
Provisions for liabilities	17	**-**	(0.8)
Net current liabilities		**(335.0)**	(45.4)
Total assets less current liabilities		**1,115.8**	1,326.8
Creditors: amounts falling due after more than one year	16	**(699.6)**	(965.0)
Derivative financial liabilities	22	**(6.8)**	(12.8)
Deferred tax liabilities	19	**(79.8)**	(78.8)
Net assets		**329.6**	270.2
Capital and reserves			
Called up share capital	20	**62.0**	62.0
Profit and loss account		**268.2**	208.8
Hedge reserve		**(0.6)**	(0.6)
Equity Shareholders' funds		**329.6**	270.2

These Financial Statements were approved by the Directors on 23 July 2021 and signed on their behalf by:

Gregor Alexander (Jul 23, 2021 14:25 GMT+1)

Gregor Alexander
Director
Company registered number: SC213460

Scottish Hydro Electric Power Distribution plc

Statement of Changes in Equity
for the year ended 31 March 2021

	Share capital £m	Retained earnings £m	Hedge reserve £m	Total equity £m
Balance at 1 April 2019	**62.0**	**238.9**	**(0.6)**	**300.3**
Profit for the year	-	44.8	-	44.8
Total comprehensive income for the year	**-**	**44.8**	**-**	**44.8**
Credit in respect of employee share awards	-	1.7	-	1.7
Dividends paid (note 9)	-	(85.0)	-	(85.0)
Adjustment in relation to historical depreciation (i)	-	8.4	-	8.4
Balance at 31 March 2020	**62.0**	**208.8**	**(0.6)**	**270.2**
Balance at 1 April 2020	**62.0**	**208.8**	**(0.6)**	**270.2**
Profit for the year	-	57.4	-	57.4
Total comprehensive income for the year	**-**	**57.4**	**-**	**57.4**
Credit in respect of employee share awards	-	2.0	-	2.0
Balance at 31 March 2021	**62.0**	**268.2**	**(0.6)**	**329.6**

(i) The adjustment in relation to historical depreciation is presented net of deferred tax.

Scottish Hydro Electric Power Distribution plc

Cash Flow Statement
for the year ended 31 March 2021

	Note	2021 £m	2020 £m
Operating profit		**98.8**	100.0
Depreciation on property, plant and equipment		**52.1**	49.6
Amortisation of intangible assets		**3.2**	2.8
Loss on disposal of property, plant and equipment		**4.7**	5.5
Movement on operating derivatives		**(3.9)**	7.4
Charge in respect of employee share awards		**2.0**	1.7
Customer contributions and capital grants released		**(3.3)**	(3.3)
Cash generated from operations before working capital movements		**153.6**	163.7
(Increase) in debtors		**(27.9)**	(18.3)
Increase in creditors		**48.7**	21.1
Movement in intercompany		**(92.5)**	(143.9)
Decrease/ (increase) in stock		**0.3**	(0.3)
Increase/(decrease) in provisions		**(0.8)**	0.8
Cash generated from operations		**81.4**	23.1
Interest paid		**(29.1)**	(26.6)
Taxes paid		**(12.5)**	(22.0)
Net cash from operating activities		**39.8**	(25.5)
Purchase of property, plant and equipment		**(134.4)**	(131.1)
Purchase of intangible assets		**(5.4)**	(8.4)
Net cash from investing activities		**(139.8)**	(139.5)
Dividends paid to company's equity holders	**9**	**-**	(85.0)
New borrowings	**18**	**100.0**	250.0
Net cash from financing activities		**100.0**	165.0
Net Increase/(decrease) in cash and cash equivalents		**-**	-
Reconciliation of net cash flow to movement in net funds			
Decrease in cash in the year		**-**	-
Net cash at start of the year		**-**	-
Net cash at end of the year		**-**	-

Scottish Hydro Electric Power Distribution plc

Notes on the Financial Statements
for the year ended 31 March 2021

1 Significant accounting policies

The Company is a public company incorporated, domiciled, and registered, in Scotland. Its registration number is SC213460, and registered office is Inveralmond House, 200 Dunkeld Road, Perth, PH1 3AQ.

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's Financial Statements.

Basis of preparation
The Financial Statements have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including Financial Reporting Standard 101 (Reduced Disclosures) (“FRS 101”) as issued by the Financial Reporting Council.

In these Financial Statements, the Company has applied the exemptions available under FRS 101 in respect of the following disclosures:
- The effect of new, but not yet effective, IFRSs;
- Related party disclosures; and
- Comparative period reconciliations for property, plant and equipment, intangible assets and share capital.

As the consolidated Financial Statements of SSE plc include the equivalent disclosure, the Company has also taken advantage of the exemptions, under FRS 101, available in respect of the following disclosures:
- Certain disclosures, required by IAS 36 *Impairment of assets,* in respect of the impairment of goodwill and intangible assets;
- Certain disclosures, required by IFRS 13 *Fair Value Measurement* and IFRS 7 *Financial Instruments Disclosure* and IFRS 15 *Revenue from Contracts from Customers*; and
- Certain disclosures, required by IFRS 16 *Leases*.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these Financial Statements.

The Company has not included employee share based payments disclosures on the basis of materiality.

The Directors consider that the Company has adequate resources to continue in operational existence for the period to 31 December 2022. The Financial Statements are therefore prepared on a going concern basis.

In making their assessment the Directors have considered the arm’s length intercompany funding from other companies with the SSE plc Group and the Group’s commitment not to request repayment of intergroup funding, unless the company has the reserves to do so for the period to 31 December 2022. In managing the liquidity of the Company, the Directors look to blend intergroup and external debt to create a balance of maturity, term and rate.

In assessing the financial strength of the Group, the Directors considered the cash surplus of £1.6bn at 31 March 2021, the committed bank facilities of £1.5bn maintained by the Group, the current commercial paper market conditions, the assumption the Group will be able to refinance maturing debt, the success of the disposal programme as well as sensitivities on future cashflow projections that reflect the impact of the coronavirus pandemic, the Group’s credit rating, and the successful issuance of £2.5bn of medium- to long-term debt and Hybrid equity during the year. The Directors also considered mitigating actions available to the Group under downside scenarios including not calling the £1.0bn Hybrid debt instruments due in September 2022, non-essential capex postponement and refinancing of maturing debt. In considering these factors, the Directors satisfied themselves that the Group has sufficient headroom to continue as a going concern.

The Company is in a net current liability position of £335.0m as at the financial year end.

1 Significant accounting policies (*continued*)

Basis of preparation *(continued)*
The Group have provided a letter of support confirming it will provide support for a period of 12 months from the date of signing of these accounts where required. The Directors are satisfied that the Group has the ability to provide this support, should it be required.

Having reviewed the Company's current performance, and the financial strength of the Group, the Directors are satisfied that the Group, and the company itself, will remain funded for the foreseeable future. The Directors have concluded it is appropriate for the Financial Statements to be prepared on a going concern basis.

Further details of the Company's liquidity position and going concern review, including the potential impacts of coronavirus, are provided on page 19.

Revenue
Use of Electricity Networks
Revenue from use of electricity networks is derived from the allowed revenue as defined by the parameters in the electricity distribution licence, which informs the tariffs we set.

Electricity distribution revenue recognised is based on the volume of electricity distributed "over time", as use of the distribution service is determined by the customer, and the set customer tariff. Where this revenue differs from the allowed revenue, there may be an over- or under-recovery of revenue which will be reflected in future financial year's allowed revenue as set out in the regulatory licence. No accounting adjustments are therefore made for over- or under-recoveries in the year that they arise.

Network contracted services
Where the Company has an ongoing obligation to provide contracted services (such as for network distribution connections), revenues are recognised "over time" evenly across the expected contractual service period in line with the customer receiving and consuming the benefits of that service. Any assets constructed in order to deliver the service are capitalised and depreciated over their useful life. Any payments received from a customer in advance of providing the contracted service are deferred on the balance sheet.

Foreign currencies
Transactions in foreign currencies are translated to the Company's functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the profit and loss account except for differences arising on the retranslation of qualifying cash flow hedges, which are recognised in other comprehensive income.

Research
Expenditure on research activities is recognised in the profit and loss account as an expense as incurred.

Taxation
Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised directly in equity or other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

1 Significant accounting policies (*continued*)

Taxation *(continued)*
A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised.

Property, plant and equipment
Property, plant and equipment (PPE) is stated at cost less accumulated depreciation and accumulated impairment losses.

Depreciation is charged to the profit and loss account on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. The estimated useful lives are as follows:

	Years
Network assets:	
Underground and subsea cables, overhead lines	5 to 80
Non-operational assets:	
Fixtures, equipment, plant and machinery, vehicles and mobile plant	5 to 10

Assets held under leasing arrangements are recognised as right-of-use assets and are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, over the term of the relevant lease.

An item of PPE is derecognised on disposal. Where no future economic benefits are expected to arise from the continued use of an item of PPE, the asset is fully written off.

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

Intangible assets
Intangible assets are stated at cost less accumulated amortisation and accumulated impairment losses.

Included within intangible assets are application software license fees, software development work, software upgrades and purchased PC software packages. Amortisation is charged on a straight line basis over 10 years and is included within distribution costs in the profit and loss account.

The carrying amounts of the Company's intangible assets are reviewed at each reporting date to determine whether there is any indication of impairment. Where indicators of impairment are identified, the carrying value of those assets is compared to the recoverable amount. An impairment loss is recognised where it is considered that recoverable amounts are less than the carrying value of those assets. For intangible assets with an indefinite life or which are not yet ready for use, the test for impairment is carried out annually in accordance with IAS 36.

Capitalised interest
Interest directly attributable to the acquisition, construction or production of major capital projects, which are projects that necessarily take a substantial period of time to get ready for their intended use, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use, and depreciated as part of the total cost over the useful life of the asset.

Leases
At lease commencement date, the Company recognises a right-of-use-asset and a lease liability on the balance sheet. The right-of-use asset is measured at cost, which is made up of the initial measurement of the lease liability and any lease payments made in advance of the lease commencement date.

The Company depreciates the right-of-use assets on a straight line basis from the lease commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The Company also assesses the right-of-use asset for impairment when such indicators exist.

1 Significant accounting policies (*continued*)

Leases *(continued)*
At the commencement date, the Company measures the lease liability at the present value of the lease payments unpaid at that date, discounted using the Company's incremental borrowing rate.

Government grants
Government grants towards Innovation projects are recognised as income over the period necessary to match them with the related costs, for which they are intended to compensate, on a systematic basis. Grants related to income are presented separately as other income in the profit and loss. Capital grants are recorded as deferred income and released to the profit and loss account over the estimated life of the asset.

Stocks
Stocks are stated at the lower of cost and net realisable value.

Restricted Cash
Restricted cash represents amounts received from Distribution Network Operators / National Grid in line with annual Ofgem Funding Directions for Innovation projects, and security deposits received from customers in respect of connections projects. The use of Innovation related cash is restricted and can only be used for the purpose of the project. Security deposit cash is ring fenced and held on behalf of National Grid until either returned to the customer on completion of the project or matured in respect of customer cancellation. The balances are not remitted to SSE plc as part of the Group's central treasury operations. This is not considered to be cash and cash equivalents.

Provisions
A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Pensions
Some of the Company's employees are members of a group wide defined benefit pension plan. As there is no contractual agreement or stated group policy for charging the net defined benefit cost of the plan to participating entities, the net defined benefit cost of the pension plan is recognised fully by the sponsoring employer, which is another member of the Group. The Company then recognises a cost equal to its contribution payable for the period. Obligations for contributions to defined contribution pension plans are recognised as an expense in the profit and loss account in the periods during which services are rendered by employees.

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

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

The costs associated with the other main employee schemes, the Share Incentive Plan and the Deferred Bonus Scheme, are recognised over the period to which they relate.

1 Significant accounting policies (*continued*)

Derivative financial instruments and hedging
Derivative financial instruments are recognised at fair value. The gain or loss on re-measurement to fair value is recognised immediately in profit or loss. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged.

Significant judgements and estimates
There are no other significant judgements or estimates in the year than those noted above.

2 Analysis of Revenue

An analysis of the Company's revenue by business segment is set out below:

	General use of electricity networks £m	Network connections services £m	Out of area network activity £m	Metering income £m	Other revenue £m	Total £m
Distribution revenue at 31 March 2021	**319.4**	**5.9**	**4.6**	**0.9**	**11.6**	**342.4**
Distribution revenue at 31 March 2020	313.1	4.3	4.6	1.0	13.2	336.2

The existence of each segment is fundamental to the successful operation of the distribution network. Each segment has similar economic characteristics and therefore the Directors assess the Company has one reportable operating segment. The Company generates revenue for the construction, maintenance and renovation of the distribution network in the north of Scotland, responsible for the supply of electricity to over 740,000 homes and businesses. The Company also provides electricity connections providing essential and safe access to the distribution network. Each segment represents an essential element of the network, allowing customers to gain and maintain supply of electricity and therefore the Directors assess that the Company has one reportable operating segment. As such, the Company does not place reliance with any single key customer. The Company continues to operate under the RIIO-ED1 price control which runs for eight years from 1 April 2015 until 31 March 2023.

The Company also recognised other income relating to government grants of £0.8m in the year. This does not equate to other revenue denoted in the analysis above.

3 Expenses and auditor's remuneration

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

	2021 £m	2020 £m
Depreciation of property, plant and equipment (note 10)	**52.1**	49.6
Amortisation of intangible assets (note 11)	**3.2**	2.8
Lease charges (i)	**0.2**	0.2
Loss on disposal of PPE (ii)	**4.7**	5.5
Release of deferred income in relation to customer contributions and capital grants	**(3.2)**	(3.3)
Government grants related to income	**(0.8)**	-
Net management fees in respect of services provided by group companies	**12.7**	14.6
Research costs	**2.2**	0.8
Exceptional restructuring costs (note 4)	**-**	1.7

(i) Represents the expense of leases with a duration of 12 months or less, leases deemed to be "low value" and variable lease payments which do not depend on an index or rate with £0.2m *(2020: £0.2m)* charged in the current year.

3 Expenses and auditor's remuneration *(continued)*

(ii) Includes £3.3m of project payments capitalised in the prior period. Following management review of capitalised project spend, a revision to PPE and Distribution costs has been recorded during the period. The cumulative effect on current year operating profit in respect of prior periods is £3.3m. It has been assessed that the cumulative effect of this revision does not materially impact the prior year financial statements.

The Company incurred £0.1m of external audit fees *(2020: £0.1m)*. Included within this are audit related assurance service fees of £0.01m *(2020: £0.01m)*.

4 Exceptional restructuring costs

The provision for unsettled redundancy costs attributable to the prior year restructuring programme has been fully utilised during the year.

	2021	2020
	£m	£m
Redundancy costs	**-**	1.7

5 Staff costs and numbers

	2021	2020
	£m	£m
Staff costs:		
Wages and salaries	**59.2**	57.3
Social security costs	**6.5**	6.3
Share based remuneration	**2.0**	1.7
Pension costs	**11.2**	10.9
	78.9	76.2
Less charged as capital expenditure	**(27.7)**	(24.6)
	51.2	51.6

Employee numbers

	2021	2020
	Number	Number
Customer facing staff	**497**	472
Support staff	**990**	926
Total staff employed at 31 March	**1,487**	1,398

Average employee numbers	**2021**	2020
	Number	Number
Customer facing staff	**489**	461
Support staff	**999**	960
Total monthly average number of people employed by the Company during the year	**1,488**	1,421

5 Staff costs and numbers *(continued)*

	2021	2020
	£m	£m
Directors remuneration	**6.1**	4.9

The total remuneration received by the Directors for qualifying and non-qualifying services including amounts paid and receivable under long term incentive schemes during the year was £6.1m (*2020: £4.9m*). The total attributable to the highest paid Director is £2.2m *(2020: £1.7m)*. The above value is for 12 Directors (*2020: 11*), 10 of whom were remunerated via another Group company in the year. A value of services to the Company for these Directors cannot be determined, therefore the above value reflects the remuneration received for services to the SSE Group as a whole.

The aggregate of amounts paid and receivable under long term incentive schemes for Directors is £2.2m *(2020: £1.5m*), of which £1.1m *(2020: £0.5m)* is due to the highest paid Director. Total company pension contributions of £0.1m (*2019: £nil*) were made to a money purchase scheme on behalf of the Directors.

10 *(2020: 7)* Directors exercised share options in the parent's shares during the year.

The highest paid Director exercised and received shares under a long-term incentive scheme in the year.

	Number of directors	
	2021	2020
Retirement benefits are accruing to the following number of Directors under:		
Defined benefit schemes	**4**	5

6 Interest receivable and similar income

	2021	2020
	£m	£m
Movement on financing derivatives	**3.3**	-

7 Interest payable and similar charges

	2021	2020
	£m	£m
Interest payable to group companies	**26.5**	25.9
Bank loans and overdrafts	**4.7**	6.2
Interest on lease liabilities	**0.3**	0.2
Movement on financing derivatives	**-**	3.1
	31.5	35.4

8 Taxation

	2021	2020
	£m	£m
UK corporation tax		
Current tax on income for the period	**12.7**	14.5
Adjustment in respect of prior periods	**(0.5)**	(1.5)
Total current tax charge	**12.2**	13.0
Deferred tax (see note 19):		
Origination and reversal of temporary differences	**0.8**	(2.0)
Adjustment in respect of prior periods	**0.2**	0.5
Effect of change in tax rate	**-**	8.3
Total deferred tax	**1.0**	6.8
Total tax on profit	**13.2**	19.8

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

	2021	2020
	£m	£m
Profit before taxation	**70.6**	64.6
Tax on profit at standard UK corporation tax rate of 19% *(2020: 19%)*	**13.4**	12.3
Effects of:		
Adjustment in respect of previous periods	**(0.3)**	(0.9)
Other items	**0.1**	0.1
Effect of change in tax rate on deferred tax	**-**	8.3
Total tax charge for year	**13.2**	19.8

The Government announced in the Budget on 3 March 2021 that the main rate of corporation tax will increase to 25% for the financial year beginning 1 April 2023. Prior to this date, the rate of corporation tax will remain at 19%. The increase to 25% rate was not substantively enacted at 31 March 2021, therefore the Company has continued to measure deferred tax balances at 19%. The Company has estimated that the increase to 25% would increase the Company's deferred tax liabilities by £25.2m.

Finance Bill 2021 also included draft legislation in respect of Capital Allowance 'Super-deductions' of 130% in respect of General Pool plant and machinery, alongside First Year Allowances of 50% for Special Rate Pool plant and machinery for the two years commencing 1 April 2021. The Company expects these changes, which have not yet been enacted, to significantly increase the deduction for Capital Allowances in the financial years ending 31 March 2022 and 31 March 2023. It is not yet possible to quantify the financial impact of these changes as guidance has yet to be issued by HMRC as to how they will apply.

9 Dividends

	2021	2020
	£m	£m
Amounts recognised as distributions from equity:		
Final dividend of nil *(2020: 137.1p)* per share	**-**	85.0

No dividend was declared in the year ended 31 March 2021 (*2020*: *£85.0m*). The final dividend for the previous year was approved on 20 February 2020 and paid to shareholders on 30 March 2020.

Scottish Hydro Electric Power Distribution plc

Notes on the Financial Statements *(continued)*
for the year ended 31 March 2021

10 Property, plant and equipment

	Network Assets	Assets under the course of construction (AUC)	Land and Buildings	Vehicles and miscellaneous equipment	Total
	£m	**£m**	**£m**	**£m**	**£m**
Cost:					
At 1 April 2020	2,478.5	22.6	4.7	90.9	2,596.7
Additions	-	132.4	0.8	-	133.2
Transfers from AUC to fully commissioned	124.6	(128.1)	-	3.5	-
Disposals	(5.2)	-	-	-	(5.2)
At 31 March 2021	**2,597.9**	**26.9**	**5.5**	**94.4**	**2,724.7**
Accumulated depreciation:					
At 1 April 2020	(1,176.5)	-	(0.2)	(76.4)	(1,253.1)
Charge for the year	(47.1)	-	(0.3)	(4.7)	(52.1)
Disposals	0.5	-	-	-	0.5
At 31 March 2021	**(1,223.1)**	**-**	**(0.5)**	**(81.1)**	**(1,304.7)**
Net book value:					
At 31 March 2021	**1,374.8**	**26.9**	**5.0**	**13.3**	**1,420.0**
At 31 March 2020	1,302.0	22.6	4.5	14.5	1,343.6

The above property, plant and equipment includes £1.4m *(2020: £1.4m)* capitalised interest. No interest was capitalised in either the current or prior year. This is depreciated annually according to the useful economic life of the asset to which the capitalised interest relates.

Included in the above line items are right-of use assets over the following:

	Land and Buildings £m
Cost:	
At 31 March 2019	-
Recognised on adoption of IFRS 16 on 1 April 2019	4.7
At 31 March 2020	4.7
Additions	0.8
At 31 March 2021	**5.5**
Depreciation:	
At 31 March 2019	-
Charge for the year	(0.2)
At 31 March 2020	(0.2)
Charge for the year	(0.3)
At 31 March 2021	**(0.5)**
Net book value:	
At 31 March 2021	**5.0**
At 31 March 2020	4.5

11 Intangible assets

	Assets in development £m	IT Software £m	Total £m
Cost:			
At 1 April 2020	4.9	33.6	38.5
Additions	3.4	2.0	5.4
At 31 March 2021	**8.3**	**35.6**	**43.9**
Amortisation:			
At 1 April 2020	-	(9.9)	(9.9)
Charge for the year	-	(3.2)	(3.2)
At 31 March 2021	**-**	**(13.1)**	**(13.1)**
Net book value:			
At 31 March 2021	**8.3**	**22.5**	**30.8**
At 31 March 2020	4.9	23.7	28.6

12 Stocks

	2021 £m	2020 £m
Raw materials and consumables	**2.3**	2.6

13 Debtors

	2021 £m	2020 £m
Trade debtors	**19.0**	18.2
Prepayments and accrued income	**54.7**	40.5
Corporation tax debtor	**0.3**	-
Contract related receivables	**4.8**	5.3
Amounts owed by group undertakings	**19.1**	7.4
	97.9	71.4

Contract related receivables relate to costs incurred on non-capital networks projects. These projects are performed at the customer's request and are paid for in full directly by the customer. The projects are partially completed at the financial year end, the costs being recognised as contract related receivables and the related income received from the customer being held within contract related liabilities at the balance sheet date.

14 Restricted cash

	2021	2020
	£m	£m
Restricted cash	**13.4**	-

Restricted cash consists of amounts received to fund Innovation projects as well as security deposits received from customers in respect of DUOS and Connections activity. Innovation cash is received from Distribution Network Operators (DNOs) to fund the Resilience at Work (RAAS) Ofgem's Networks Innovation Competition funding. These bank accounts contain amounts received from DNOs / National Grid in line with annual Ofgem Funding Directions. The use of the cash is restricted and can only be used for the purpose of the project. Security deposit cash is held for customer connections projects and is ring fenced. The money is either returned to the customer on completion of the connection or matured in respect of cancellation. The restricted cash balance has not been remitted to SSE plc as part of the Group's central treasury operations. Any non-restricted cash generated by the Company is remitted to or obtained from the Group or SSE Services plc. This is not considered to be cash and cash equivalents for the purposes of the cash flow statement.

15 **Creditors:** amounts falling due within one year

	2021	2020
	£m	£m
Trade creditors	**7.5**	3.2
Amounts owed to group undertakings	**82.4**	67.5
Other creditors	**13.8**	12.4
Loans due to ultimate parent (note 18)	**300.0**	-
Obligations under leases	**0.3**	0.3
Accruals	**31.0**	23.1
Contract related liabilities (i)	**14.9**	12.1
	449.9	118.6

(i) Current contract related liabilities include customer contributions of £3.3m *(2020: £3.4m).* Revenue recognised in the reporting period of £2.5m was included in contract liabilities at the beginning of the period.

The amounts owed to Group undertakings include amounts advanced to the Company by its ultimate parent SSE plc. Interest on these balances is charged at 4.01% *(2020: 4.06%).*

16 **Creditors:** amounts falling due after more than one year

	2021	2020
	£m	£m
Loans and borrowings (note 18)	**147.6**	146.2
Loans due to ultimate parent (note 18)	**350.0**	550.0
Obligations under leases	**5.8**	5.4
Contract related liabilities (i)	**196.2**	167.7
Amounts owed to group undertakings	**-**	95.7
	699.6	965.0

(i) Non-current contract related liabilities include customer contributions of £37.7m *(2020: £39.4m).*

The amounts owed to Group undertakings include amounts advanced to the Company by its ultimate parent SSE plc. Interest on these balances is charged at 4.01% *(2020: 4.06%).*

17 Provisions for other liabilities

	2021	2020
	£m	£m
At 1 April	**0.8**	-
Additions in the year	**-**	0.8
Utilised during the year	**(0.8)**	-
At 31 March	**-**	0.8

The prior year provision for unsettled restructuring costs has been fully utilised in the year.

18 Interest bearing loans and borrowings

This note provides information about the contractual terms of the Company's interest bearing loans and borrowings which are held at amortised cost.

	Weighted Average Interest Rate 2021 %	Weighted Average Interest Rate 2020 %	**2021 £m**	2020 £m
Creditors: falling due within one year				
5.90% Loan Stock repayable to SSE plc on 31 March 2022	**5.90**	-	**300.0**	-
Creditors: falling due in more than one but not more than two years				
5.90% Loan Stock repayable to SSE plc on 31 March 2022	**-**	5.90	**-**	300.0
Creditors: falling due more than five years				
2.125% Loan Stock repayable to SSE plc on 31 March 2036	**2.13**	-	**100.0**	-
2.250% Loan Stock repayable to SSE plc on 29 September 2034	**2.25**	2.25	**250.0**	250.0
1.4296% Index linked bond repayable on 20 October 2056	**2.04**	2.04	**147.6**	146.2
			497.6	396.2
			797.6	696.2

The effective interest rate is equal to the weighted average interest rate for all borrowings.

19 Deferred tax liabilities

Deferred tax (assets) and liabilities are attributable to the following:

	Assets		**Liabilities**		**Net**	
	2021	2020	**2021**	2020	**2021**	2020
	£m	£m	**£m**	£m	**£m**	£m
Accelerated capital allowances	**-**	-	**79.8**	79.5	**79.8**	79.5
Other timing differences	**(0.2)**	(0.2)	**-**	-	**(0.2)**	(0.2)
Fair value movement on derivatives	**-**	(0.5)	**0.2**	-	**0.2**	(0.5)
Net tax liabilities	**(0.2)**	(0.7)	**80.0**	79.5	**79.8**	78.8

19 Deferred tax liabilities (*continued*)

	1 April 2020	**Opening balance adjustment (i)**	**Recognised in income**	**Recognised in equity**	**31 March 2021**
	£m	**£m**	**£m**	**£m**	**£m**
Movement in deferred tax during the year	**78.8**	**-**	**1.0**	**-**	**79.8**

	1 April 2019	Opening balance adjustment (i)	Recognised in income	Recognised in equity	31 March 2020
	£m	£m	£m	£m	£m
Movement in deferred tax during prior year	70.2	(0.2)	6.8	2.0	78.8

(i) An opening balance adjustment totalling £0.2m was made on adoption of IFRS 16 at 1 April 2019.

20 Equity

Share capital

	2021	2020
	£m	£m
Equity:		
Allotted, called up and fully paid:		
62,000,000 ordinary shares of £1.00 each	**62.0**	62.0

Hedge reserve

The hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedge derivative instruments related to hedged transactions that have not yet occurred.

21 Pensions

8% *(2020: 9%)* of the Company's employees are members of the Scottish Hydro-Electric Pension Scheme which provides defined benefits based on final pensionable pay. As there is no contractual agreement or stated group policy for charging the net defined benefit cost of the plan to participating entities, the net defined benefit cost of the pension plan is recognised fully by the sponsoring employer, which is another member of the Group.

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

The Company's share of the total contribution payable to the pension schemes during the year was £11.2m *(2020: £10.9m)*.

22 Derivatives and financial instruments

The Group's Treasury department is responsible for managing the banking and liquidity requirements of the Company, risk management relating to interest rate and foreign exchange exposures, and for managing the credit risk relating to the banking counterparties with which it transacts. Short term liquidity is reviewed daily by the department while longer term liquidity position is reviewed on a regular basis by the Group Board. The department’s operations are governed by policies determined by the Group Board and any breaches of these policies are reported to the Tax and Treasury Committee and the Group's Audit Committee. The Group’s policy is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to either the Group or Company’s reputation.

22 Derivatives and financial instruments *(continued)*

The Group holds committed bank facilities of £1.5bn at 31 March 2021 which could be made available to the Company if required. The Directors have considered sensitivities on future cashflow projections resulting from the coronavirus pandemic and given the facilities available, including those held at Group and Company level, the Directors have concluded that the Company has sufficient headroom to continue as a going concern.

(i) Commodity risk

The Company is exposed to the commodity risk that is associated with forward contract activity in the buying (and selling) of commodities. The risk is derived from the Company's oil option contract which has been entered into with the aim of meeting the future demand requirements of its energy supply business.

Throughout the year the Company was exposed to market risk associated with fluctuations in the market price of oil as well as the volumetric risk caused by unplanned changes in the load and output of the portfolio. Short-term exposures will arise from the requirement to match volumes of procured oil with the demand of domestic and business supply customers. This can vary from expectation and result in a requirement to close the contracted positions at unfavourable prices.

The risk management activity is carried out by the Group's Energy Portfolio Management ("EPM") business which manages the exposure to energy commodity price movements on behalf of the Company. The strategy has been to manage all exposures to commodity risk through volumetric limits and to measure the exposure by use of Value at Risk (VaR) models which considers exposures in all commodities. The exposure is subject to financial limits established by the Board and managed by reference to guidance agreed by the Risk Committees. Exposures are reported to the Committees on a monthly basis and to the Board when certain trigger levels are exceeded.

The Company accounting policy is to record the operating derivative at fair value through the profit and loss.

(ii) Interest rate risk

Exposure to interest rate risk arises in the normal course of the Company's business. Interest rate risk derives from the Company's exposure to changes in value of an asset or liability or future cash flows through changes in interest rates. Derivative financial instruments are entered into to hedge exposure to risk. The objectives and policies for holding or issuing financial instruments and similar contracts, and the strategies for achieving those objectives that have been followed during the year are explained below.

The Company's policy is to manage this risk by stipulating that a minimum of 50% of borrowings be subject to fixed rates of interest, either directly through the debt instruments themselves or through the use of derivative financial instruments. The floating rate borrowings are provided by banks including the European Investment Bank (EIB). Such instruments include interest rate swaps. These practices serve to reduce the volatility of the Company's financial performance.

Although interest rate derivatives are primarily used to hedge risk relating to current borrowings, under certain circumstances they may also be used to hedge future borrowings. Any such pre-hedging is unwound at the time of pricing the underlying debt, either through cash settlement on a net present value basis or by transacting offsetting trades. The floating rate borrowings comprise loan instruments from the EIB.

The impact of a change in interest rates is dependent on the specific details of the financial asset or liability in question. Changes in fixed rate financial assets and liabilities, which account for the majority of cash, loans and borrowings, are not measured at fair value through the income statement. In addition to this, changes to fixed-to-floating hedging instruments which are recorded under cash flow hedge accounting also do not impact the income statement. Changes in variable rate instruments and hedging instruments and hedged items recorded under fair value hedge accounting are recorded through the income statement. The exposure measured is therefore based on variable rate debt and instruments.

22 Derivatives and financial instruments *(continued)*

(iii) Fair values

The fair values of the Company's financial assets and financial derivatives, and the carrying amounts in the balance sheet are analysed below. Balances included in the analysis of primary financial assets and liabilities include cash and cash equivalents, loans and borrowings, trade debtors and trade creditors, all of which are disclosed separately.

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

	2021 Carrying value £m	**2021 Fair Value £m**	2020 Carrying value £m	2020 Fair Value £m
Financial Assets				
Trade and intercompany debtors	**38.1**	**38.1**	25.6	25.6
Derivative financial assets	**1.3**	**1.3**	-	-
Financial Liabilities				
Trade and intercompany creditors	**89.9**	**89.9**	70.7	70.7
Long-term intercompany	**-**	**-**	95.7	95.7
Loans and borrowings	**147.6**	**252.1**	146.2	199.7
Loans due to ultimate parent	**650.0**	**652.1**	550.0	590.2
Derivative financial liabilities	**6.8**	**6.8**	12.8	12.8

Fair values have been determined with reference to closing market prices. Unless otherwise stated, carrying value approximates fair value.

Financial and operating derivative instruments - disclosure
For disclosure purposes, derivative financial instruments are classified into two categories – operating derivatives and financing derivatives. The Company utilises financing derivatives in the form of interest rate derivatives. Operating derivatives relate to energy option contracts for oil stored at the Shetland Gas Terminal, which are all held at fair value through the profit and loss account. Non-hedge accounted contracts are treated as held for trading (MTM). The carrying value is the same as the fair value for all instruments. All balances are stated gross of associated deferred taxation.

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

23 Capital commitments

	2021 £m	2020 £m
Contracted but not provided for	**23.5**	22.8

24 Commitments and contingencies

The Company has provided a guarantee in relation to £300m Euro bonds (expiry 2022) held by the Group. This guarantee has been provided jointly with Scottish Hydro Electric Transmission plc.

Scottish Hydro Electric Power Distribution plc

Notes on the Financial Statements *(continued)*
for the year ended 31 March 2021

25 Net debt

Reconciliation of movements in financing liabilities

	Financing Cash Flows			Non Cash			
	At 31 March 2020 £m	**New Borrowings £m**	**Repayment of lease creditor £m**	**Fair Value movement £m**	**New lease liabilities £m**	**Reclassification £m**	**At 31 March 2021 £m**
Loan Stock	550.0	100.0	-	-	-	(300.0)	350.0
Index Linked Bond	146.2	-	-	1.4	-	-	147.6
Total long-term liabilities	**696.2**	**100.0**	**-**	**1.4**	**-**	**(300.0)**	**497.6**
Loan stock	-	-	-	-	-	300.0	300.0
Total short-term liabilities	**-**	-	-	-	-	**300.0**	**300.0**
Lease liabilities	5.7	-	(0.4)	-	0.8	-	6.1
Total loans and borrowings	**701.9**	**100.0**	**(0.4)**	**1.4**	**0.8**	**-**	**803.7**

		Financing Cash flows				Non cash	
	At 31 March 2019 £m	New Borrowings £m	Repayment of borrowings £m	Repayment of lease creditor £m	Fair Value movement £m	Lease liabilities £m	At 31 March 2020 £m
Loan Stock	300.0	250.0	-	-	-	-	550.0
Index Linked Bond	142.4	-	-	-	3.8	-	146.2
Total Long-term liabilities	442.4	250.0	-	-	3.8	-	696.2
Lease liabilities	-	-	-	(0.5)	-	6.2	5.7
Total loans and borrowings	442.4	250.0	-	(0.5)	3.8	6.2	701.9

26 Related undertakings

The related undertakings in which the Company has a shareholding are listed below:

Company Name	Relation	Country of incorporation	Registered address (key)	2021 Holding %	2020 Holding %	Principal activity
Electralink Limited	Investment	England and Wales	B	**4.89**	4.89	Data Transfer Service Operator
Gemserv Limited	Investment	England and Wales	A	**2.78**	2.78	Market Design, Governance and Assurance Service Provider
DCUSA Limited	Investment	England and Wales	B	**1.67**	1.69	Billing Framework Operator
MRA Service Company Limited	Investment	England and Wales	A	**0.36**	0.39	Metering Point Administration Services Operator
Smart Energy Code Company Limited	Investment	England and Wales	A	**0.33**	0.34	Smart Metering Implementation Management

Registered Address Key

Address	Reference
8 Fenchurch Place, London, EC3M 4AJ	A
Northumberland House, 303 - 306 High Holborn, London, England, WC1V 7JZ	B

The Directors have reviewed the recoverability of the carrying value of the investment at 31 March 2021 and are satisfied that the carrying amount is not more than the recoverable amount.

27 Ultimate parent company

The Company is a subsidiary of SSE plc, which is the ultimate parent company and is registered in Scotland. The largest and smallest Group in which the results of the Company are consolidated is that headed by SSE plc. The consolidated Financial Statements of the Group (which include those of the Company) are available from the Company Secretary, SSE plc, Inveralmond House, 200 Dunkeld Road, Perth, PH1 3AQ or by accessing the Company's website at www.sse.com.