



SCOTTISHPOWER

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DIRECTORS' REPORT

The directors present their report and audited Accounts for the year ended 31 December 2012.

ACTIVITIES AND REVIEW

Scottish Power UK plc, ("the company"), registered company number SC117120, principally acts as the holding company of the Scottish Power UK plc group, ("the group"), whose activities comprise the generation, transmission, distribution, gas storage, energy management and supply of electricity and gas in the United Kingdom ("UK"). The four businesses operated by the group during the year were Energy Networks, Energy Wholesale, Energy Retail and Renewables.

Energy Networks includes "asset-owner companies" holding the group's regulated assets and transmission and distribution licences. In addition, a further subsidiary provides asset management expertise and conducts the day-to-day operation of the networks.

Energy Wholesale operates the generation assets of the group, with the exception of renewables, and manages the group's exposure to the UK wholesale electricity and gas markets.

Energy Retail is responsible for energy supply, the sales and marketing of electricity and gas to customers throughout the UK, together with the associated customer registration, billing and receipting processes and handling enquiries in respect of these services.

Renewables operates the group's wind-powered electricity generation assets and develops investment opportunities in renewable energy generation.

On 1 January 2012, as part of an Iberdrola group restructuring exercise, the company acquired 100% of the share capital of ScottishPower Renewable Energy Limited ("SPREL") a subsidiary of Iberdrola S.A. ("Iberdrola"). Since that date the group has been responsible for the management of the renewable energy activities of Iberdrola in the UK and Republic of Ireland. Details of this acquisition are set out at Note 34.

The company's ultimate parent company is Iberdrola which is listed on the Madrid stock exchange. The company's ultimate UK parent company is Scottish Power Limited, which is the holding company of the Scottish Power Limited group ("ScottishPower").

CORPORATE RESTRUCTURING

On 1 January 2012, as part of an Iberdrola group restructuring exercise, the company acquired 100% of the share capital of SPREL, a subsidiary of Iberdrola. This transaction is deemed to be a business combination under common control and has been accounted for under the pooling of interests method in the consolidated Accounts. Further details are described in Notes 2 and 34.

This transaction had the following effect on the consolidated results of the group for the year ended 31 December 2012:

	£m	
Revenue	12	(year to 31 December 2012)
Profit from operations	63	(year to 31 December 2012)
Net assets	1,362	(recognised at 1 January 2012)

On 1 July 2011, as part of a group restructuring exercise to align the operational structure of ScottishPower with the operational structure of the Iberdrola group, those entities within the group deemed to be part of the Energy Networks business were transferred to Scottish Power Energy Networks Holdings Limited ("SPENH") and those entities within the group deemed to be part of the Energy Wholesale and Energy Retail businesses were transferred to Scottish Power Generation Holdings Limited ("SPGH"). Both SPENH and SPGH are direct subsidiaries of the company. These transfers were undertaken at the book value of the investment and had no impact on the consolidated net profit or net assets of the group.

Similarly, on the same date, certain entities deemed to be part of the Energy Wholesale business (namely ScottishPower Energy Management Limited, ScottishPower Energy Management (Agency) Limited, ScottishPower (DCL) Limited and its subsidiaries, SP Gas Transportation Hatfield Limited and SP Gas Transportation Cockenzie Limited) were transferred from Scottish Power UK Holdings Limited ("SPUKH"), the immediate parent of the company, to SPGH for a cash consideration of £65.3 million. These transactions are deemed to be business combinations under common control and have been accounted for under the pooling of interests method in the consolidated Accounts. Further details are described in Notes 2 and 34.

Although no gain or loss arose, the transactions had the following effect on the consolidated results of the group for the year ended 31 December 2011:

	£m	
Revenue	626	(from 1 July to 31 December 2011)
Loss from operations	(159)	(from 1 July to 31 December 2011)
Net assets	175	(recognised at 1 July 2011)

DIRECTORS' REPORT *continued*

KEY FACTORS AFFECTING THE BUSINESS

The businesses' objectives to manage the key drivers impacting the financial performance of the group during the year were as follows:

Energy Networks

- Deliver returns at, or in excess of allowed regulated returns
- Deliver investment programmes and operational improvements
- Improve security of supply and network performance

The objectives of the Energy Networks business must be achieved within the conditions of the Price Control review set by The Office of the Gas and Electricity Markets ("Ofgem").

Energy Wholesale

- Manage wholesale energy costs to optimise value
- Maintain flexible, reliable and available generation plant
- Deliver investment plans for short-term plant optimisation and long-term growth

Energy Retail

- Offer competitive products to customers
- Develop new, innovative routes to market
- Deliver excellent customer service across all key processes

Renewables

- Deliver onshore and offshore investment programmes efficiently
- Maximise plant availability on operational sites
- Improve efficiency of operations and reduce costs

The table below provides key non-financial information relating to the group's performance during the year.

Key performance indicators	Notes	2012	2011
Energy Networks			
Distributed energy (GWh)		35,521	35,434
System performance			
– Customer interruptions	(a)	45.7	46.2
– Customer minutes lost	(b)	46.2	47.5
Energy Wholesale and Renewables			
Plant output (TWh)			
– Combined cycle gas turbine plants		4.4	9.5
– Coal		11.2	10.3
– Renewables		2.3	–
		17.9	19.8
Energy Wholesale and Renewables			
Generating capacity (MW)			
– Thermal electric plants		5,371	5,371
– Hydroelectric plants		563	563
– Combined heat and power plants		102	102
– Wind power plants (operating capacity)	(c)	1,215	–
		7,251	6,036
Energy Retail customers (millions)			
– Electricity		3.4	3.2
– Gas		2.2	2.0
		5.6	5.2

(a) Customer interruptions are measured by the number of customers, per 100 customers, that are affected during the year by power cuts which last for three minutes or more.

(b) Customer minutes lost are measured by the average number of minutes that a customer is without power during the year due to power cuts which last for three minutes or more.

(c) In addition to wind power plant operating capacity, at the year end there was installed capacity awaiting connection of 24 MW and capacity under construction of 187 MW.

DIRECTORS' REPORT *continued*

PRINCIPAL RISKS AND RISK MANAGEMENT ACTIVITIES

ScottishPower's strategy, which is adopted by the group, is to conduct business in a manner benefiting customers through balancing cost and risk while delivering shareholder value and protecting ScottishPower's performance and reputation by prudently managing the risks inherent in the business. To maintain this strategic direction ScottishPower develops and implements risk management policies and procedures, and promotes a robust control environment at all levels of the organisation.

ScottishPower manages risk exposure in three main areas: energy market risk, credit risk and treasury risk. During 2012, the governance structure was supported by risk policies approved by the Board of Directors of Iberdrola and adopted by the Board of Directors of Scottish Power Limited ("ScottishPower Board"). ScottishPower's business risk assessment teams and the independent group Risk Management function supported the ScottishPower Board in the execution of due diligence and risk management. In addition, ScottishPower is represented at the Iberdrola Risk Management Committee to ensure that the businesses' risks are adequately assessed, monitored, mitigated and managed. Details of ScottishPower's governance structure and other relevant financial risk matters are provided in Note 4 to the group Accounts.

OPERATIONAL FINANCIAL PERFORMANCE

Overview

The table below provides key financial information relating to the group's performance during the year:

Financial Information	2012 £m	2011 £m
Revenue	7,803	6,441
Profit from operations	853	370
Net profit for the year	648	267
Total assets	13,802	9,834
Total liabilities	(10,024)	(7,748)
Net assets	3,778	2,086
Net cash flows from operating activities	1,381	964
Net debt	3,457	2,619
Net capital investment	956	545

Revenue increased primarily due to the impact of group restructuring (the inclusion of the Renewables business for the first time). There was an underlying increase in revenue mainly within Energy Retail, driven by increases in the volume of energy sold (primarily from weather impacts) and increases in the customer base and domestic and business customer tariffs. Revenue within Energy Networks also increased but decreased in Energy Wholesale mainly due to lower power sales to the wholesale market.

Procurements increased due to the impact of the group restructure (the inclusion of the Renewables business). There was also an underlying decrease in procurements mainly within Energy Wholesale and Energy Retail due to lower gas purchases from the wholesale market. Partly offsetting this in Energy Retail were increases in distribution and renewable obligation costs.

Net staff costs were in line with the prior year, with the impact of the group restructure (the inclusion of the Renewables business) as well as annual salary increases being offset by the impact of business restructures, primarily in the Energy Retail business. **Outside services** increased mainly due to the inclusion of the Renewables business. Increased activity in Energy Networks and higher IT costs within the corporate business have also impacted.

Other operating income decreased mainly due to a reduction in the value of allocated emission allowances.

Taxes other than income tax increased mainly within Energy Retail as a result of increased spending on the group's obligations for the Community Energy Saving Programme ("CESP") and for the Carbon Emissions Reduction Target ("CERT").

Depreciation and amortisation charge, allowances and provisions decreased primarily due to the 2011 impairment charge of £169 million, resulting from a reassessment of the operational life of a coal-fired power station. This was partly offset by the impact of the group restructure and the inclusion of the Renewables business.

Net finance costs were higher than prior year, mainly due to an adverse variance on the derivative position. Interest payable on group loans increased as a result of the integration of the Renewables business. These increases were partly offset by an increase in the net expected return on retirement benefit obligations. In addition, a gain recognised in the prior year on the disposal of other investments was not repeated in the current year.

The **income tax** charge for the year increased, due to an increase in taxable profits offset by the impact of reducing tax rates.

Cash and net debt

Net cash flows from operating activities increased by £417 million to £1,381 million for the year.

Overall, net debt increased to £3,457 million. The movement in net debt comprised an increase in external debt of £327 million and an increase in cash and short term deposits of £12 million. Group loans receivable increased by £943 million and group loans payable increased by £1,466 million.

DIRECTORS' REPORT *continued*

OPERATIONAL FINANCIAL PERFORMANCE *continued*

Net capital investment

ScottishPower's investment strategy is to drive the growth and development of its regulated and competitive businesses, through a balanced programme of capital investment. Cumulatively, since acquisition by Iberdrola in 2007, ScottishPower has invested £4 billion of capital expenditure.

For the year ended 31 December 2012, ScottishPower invested £956 million in its asset base. Of this, £1,039 million related to property, plant and equipment and £17 million to intangible software additions. This is offset by £100 million of customer contributions received.

Strategic plan

Since 2007 ScottishPower has been part of Iberdrola, one of the world's largest utility companies and has a significant role to play in helping Iberdrola deliver on its international strategic ambitions. The focus of the strategic plan includes optimisation of both existing assets and future investments with the aim of maximising value, as well as improving customer service levels and investing to deliver efficiency and environmental improvements. The Energy Networks investment programme, which is undertaken within the scope of regulatory price controls, continues to be a major focus, reflecting the requirement to replace ageing infrastructure to maintain a reliable energy system, as well as facilitating the connection of new renewable energy sources and the energy flows that this will create. The Renewables business is firmly committed to the responsible development of renewable energy. Planned future investment aims to progress Iberdrola's current portfolio of onshore wind as well as develop offshore wind and marine energy projects in the UK.

Investment is planned in generation to maintain ScottishPower's strong operational record and to further improve environmental performance, along with the development of new generation capacity to contribute to security of supply in the UK. In line with government policy, ScottishPower also plans to invest in the roll-out of smart meters to its Energy Retail customers. This will represent the biggest investment programme undertaken by the retail energy sector. It will provide customers with greater visibility over their energy consumption and facilitate the development of smart grids and a reduction in carbon emissions. ScottishPower are also investing to upgrade the Customer Relationship Management system within its Energy Retail business, which will deliver further improvements to customer service and efficiency, thus maintaining its competitive position in this highly competitive sector. Combined with the focus on customer satisfaction, the environment and efficiency, these investments will create value for Iberdrola shareholders and security for ScottishPower's employees and suppliers who will deliver these investments.

Some of the statements contained herein are forward looking statements and statements about Iberdrola's strategic plans. Although ScottishPower believes that the expectations reflected in such statements are reasonable, the statements are not guarantees as to future performance and undue reliance should not be placed on them.

RESULTS AND DIVIDEND

The net profit for the year attributable to the equity holders of the parent amounted to £648.1 million (2011 £267.3 million). No dividend was paid during the year (2011 £200.0 million).

CAPITAL AND DEBT STRUCTURE

The company is funded by a combination of debt and equity. All equity is held by SPUKH, the immediate parent undertaking. The funding activities of the group are centrally managed by Iberdrola group treasury. The Iberdrola group currently has liquidity of €12 billion, all of which is committed and can be used to fund group activities. During the year ended 31 December 2012, SP Manweb plc, an indirect subsidiary of the company issued a £350 million euro-sterling bond and during the year ended 31 December 2011, SPD Finance UK plc, an indirect subsidiary of the company, also issued a £350 million euro-sterling bond. Further details of the terms of these bonds can be found in Note 18. Details of the group's financial risk management policy are set out at Note 4.

UK ELECTRICITY AND GAS INDUSTRY REGULATION

Industry regulation in the UK

The principal laws governing the group's activities are the Electricity Act 1989 and the Gas Act 1986, as substantially amended and supplemented by numerous subsequent enactments, including the Gas Act 1995, the Utilities Act 2000, the Energy Act 2004, the Energy Act 2008, the Energy Act 2010, the Energy Act 2011 and various European Union ("EU") directives. A further Energy Bill was introduced into the UK Parliament in November 2012 and remains under consideration.

Other laws relating to subjects such as environmental protection, health and safety, planning and competition are also very important parts of the framework in which the group operates. These laws are enforced respectively by the Environment Agency (or, in Scotland, the Scottish Environmental Protection Agency); the Health & Safety Executive ("HSE"); local and national planning authorities; and the Office of Fair Trading ("OFT") working concurrently with Ofgem. Aspects of consumer protection are enforced by Trading Standards Authorities, the OFT and Ofgem.

The regulatory authority

The Utilities Act 2000 replaced individual gas and electricity regulators with one regulatory authority, the Gas and Electricity Markets Authority ("GEMA"), comprising a chairman and other members appointed by the Secretary of State for Energy and Climate Change. GEMA is supported by Ofgem, a non-ministerial UK Government department. The main instrument of regulation used by GEMA is the licensing regime, which in most cases requires the various aspects of the energy industry to be carried out under a licence to which standard conditions apply. In addition, there are a number of statutory obligations, known as "relevant requirements", which are enforced by GEMA as if they were licence conditions.

DIRECTORS' REPORT *continued*

UK ELECTRICITY AND GAS INDUSTRY REGULATION *continued*

The regulatory authority *continued*

GEMA's principal objective is to promote the interests of present and future consumers, wherever appropriate, by promoting effective competition. The interests of such consumers are their interests taken as a whole, including their interests in the reduction of greenhouse gases and in the security of the supply of gas and electricity to them; and before GEMA protects consumers' interests by means of competition they must consider whether an alternative course of action would better protect those interests.

In furthering this objective GEMA must ensure that all reasonable demands for electricity and gas are met, ensure that licence holders are able to finance the activities they are obliged to undertake, and contribute to the achievement of sustainable development. Numerous other duties are also required to be taken into account, but do not override the principal duties. They include the interests of customers who are disabled or chronically sick, of pensionable age, have low incomes or live in rural areas. They also include the interests of users of other utilities, promoting the efficient running of the companies in the industry, protecting the public from danger, securing a diverse and viable long term energy supply, and complying with good regulatory practice.

GEMA's functions include the granting of licences (and revoking them in certain limited circumstances), making of changes to licence conditions (including the operation of price controls for the monopoly network functions), reviewing industry code modification proposals and operating schemes for promoting renewable electricity and energy efficiency, and enforcement of the industry's obligations.

GEMA has power to impose monetary penalties for past and ongoing breaches of licence conditions and relevant requirements. Fines can be up to ten per cent of the licensee's applicable turnover.

The Secretary of State and GEMA have to provide an annual report to Parliament on the security of energy supply and also the capacity of the network to deliver that energy. This will form a key input into capacity mechanism under Electricity Market Reform ("EMR") (See below).

Licences

The companies within the group hold licences for various functions including:

- the supply of electricity;
- the generation of electricity;
- the distribution of electricity in the South of Scotland area and the Merseyside and North Wales area;
- the transmission of electricity in the South of Scotland area;
- the supply of gas;
- the shipping of gas (that is arranging for it to be introduced into, conveyed by means of or taken out of the public network); and
- the transportation of gas to certain specific sites (such as proposed new gas fired power stations).

The same company is not permitted to hold both an electricity transmission or distribution licence and an electricity supply or generation licence. Similarly, the same company is not permitted to hold a gas transporter licence and a gas supply or gas shipper licence. However, it is possible for different entities within the same group to hold such licences.

The EU third package electricity directive (2009/72/EC) sets down additional restrictions about the ownership of transmission companies. On 19 June 2012, SP Transmission Limited ("SPT") was certified by Ofgem under Article 9(9) of the Directive, with the approval of the EU Commission, on the grounds that SPT's arrangements guarantee more effective independence than the "ITO" arrangements in Chapter V of the Directive. As a result, the unbundling provisions do not apply to SPT.

The conditions of licences regulate such matters as:

- for network licensees, the quality of service and the charges that can be made;
- for supply to domestic consumers, consumer protection provisions including rules on debt and disconnection, cost reflective pricing in relation to payment methods, provision of information to consumers and on fair marketing;
- for most types of licence, rules requiring adherence to industry codes that set down the detailed technical rules for operating the industry, and providing for Ofgem to determine whether proposed changes to the codes should go ahead.

The Gas Act 1995 and Utilities Act 2000 introduced standard licence conditions to ensure that all holders of a particular licence type are normally subject to the same conditions. The Secretary of State determined the initial standard licence conditions, although subsequent modifications are made by GEMA. Under the Electricity and Gas (Internal Markets) Regulations 2011, modifications, whether to the conditions of an individual licence or to the standard conditions, no longer require any consent by the licence holders. However, the licence holder(s) in question, and certain other persons or bodies who are materially affected, can appeal the matter to the Competition Commission on matters of procedure and/or substance.

DIRECTORS' REPORT *continued*

UK ELECTRICITY AND GAS INDUSTRY REGULATION *continued*

Licences *continued*

The Energy Acts 2008, 2010 and 2011 contain clauses allowing the Secretary of State to modify licence conditions without appeal to the Competition Commission for certain specified purposes, including the introduction of smart meters, the introduction of feed-in tariffs for small scale renewable or combined heat and power generation, the creation of a renewable heat incentive, implementing assistance schemes for people at risk of fuel poverty, setting notice periods to be given for tariff changes, the limitation of excessive returns in the balancing market, setting up the "Green Deal" energy efficiency scheme, providing additional information on consumer bills and facilitating the proposed special administration regime in the event of supplier insolvency. In most cases, these powers are time limited. Changes to licence conditions can also be made without appeal to the Competition Commission in pursuance of an EU obligation, using powers in the European Communities Act 1972.

When Ofgem makes a decision on modifying an industry code which runs contrary to the views of the relevant industry governance body, the decision can, with certain exceptions, be appealed to the Competition Commission.

Competition legislation

GEMA also has concurrent powers with the OFT to apply the Competition Act 1998, the Fair Trading Act 1973 and the Enterprise Act 2002 to the energy sector in Great Britain. The Competition Act 1998 is based on Articles 81 and 82 of the European Community Treaty (now Articles 101 and 102 of the Treaty on the Functioning of the European Union) and GEMA can levy fines of up to ten per cent of turnover for breaches of the prohibitions on anticompetitive agreements or abuse of a dominant position.

Under the Enterprise Act, GEMA and the OFT have powers to initiate a market investigation where it appears that competition has been prevented, restricted or distorted in relation to commercial activities connected with the electricity or gas markets (and where it would not be more appropriate to proceed under the Competition Act 1998 or using other powers). Features that could be examined are the structure of the market (or any aspect of its structure), the conduct of companies operating within it, and the conduct of such companies' customers. The market is assessed according to a competition-based test.

The Government introduced the Enterprise & Regulatory Reform Bill in May 2012 intended to merge the Competition Commission (CC) and OFT, creating a single Competition Market Authority ("CMA"). The CMA which is expected to start operations in April 2014 will retain most of the functions and powers of the CC and OFT. The Bill is intended to give the CMA increased powers to halt and unwind mergers and conduct cross market investigations. It is also intended that the CMA will be subject to statutory timescales on first stage inquiries and investigations and second stage development of remedies.

Price controls

Prices for the sale of electricity and gas by utilities to final consumers are not controlled in Great Britain. There is no controlled tariff for certain categories of consumer, although all the major suppliers offer a system of rebates and other benefits for certain disadvantaged customers in accordance with the Warm Home Discount Regulations 2011. The total cost of the Warm Home Discount measures for the group in 2012-13 is likely to be of the order of £5 per customer account and (as with any other cost) it is open to suppliers to factor this cost into their tariffs. Ofgem has implemented licence modifications requiring any price variation by payment method to be cost reflective, but has allowed the licence condition requiring broader non-discrimination in charges to lapse. Similarly, there are no controls other than those established in the Competition Act 1998 on the level of prices charged to commercial customers or on the wholesale electricity and gas markets.

Since 29 October 2012, there has been a Transmission Constraint Licence Condition (TCLC) applicable to electricity generators. This prohibits the making of excessive gains as a result of generators making uneconomic dispatch decisions or when offering downward flexibility to the grid. Ofgem have issued guidance on their intended approach to the interpretation and enforcement of the TCLC which recognises the factors that generators are required to take into account in scheduling decisions and bid pricing. Rulings under the TCLC are subject to review by the Competition Appeals Tribunal, rather than the more limited review by the Court for other Ofgem enforcement decisions, and the condition will lapse five years after its introduction, with possible extension for a further two years.

Ofgem is carrying out a statutory consultation on the final proposals under its retail market review programme to limit the products that can be sold in the domestic energy market. The proposals include constraints on the number and make up of tariffs (with a cap of four core tariffs plus variations by parameters such as payment method, metering type and region), prescribed information requirements and requirements to notify customers about cheapest tariffs. The Government is also planning to take powers in the new Energy Bill to impose similar requirements, over-riding any possible appeal to the CC. Ofgem has also completed statutory consultation on proposed Standards of Conduct in the treatment of customers covering all aspects of the supplier-customer relationship.

The transmission and distribution networks are however recognised to be a natural monopoly. Their prices have been controlled according to a five-year formula known as RPI-X. The regulator assessed the costs of an efficient network operator and the necessary capital programme in order to calculate the return needed to meet a target return on capital. Various incentives were then added to the formula which also took account of the Retail Prices Index (RPI) and any projected efficiency improvements (-X) in order to calculate the permissible revenues for the network.

This framework is being replaced by the new "RIIO" framework (Revenue = Incentives + Innovation + Outputs). RIIO is broadly similar to RPI-X, but there are a number of important changes. These include moving to an eight year price control period (with a limited review after four years), the use of a market related index to assess the cost of debt, and the phasing in for electricity of a 45 year depreciation lifetime to replace the period of 20 years that was in use under RPI-X. Also, the process for setting the controls has changed with a "fast track" process designed to conclude the negotiation quickly for companies who submit business plans that are acceptable to Ofgem.

In transmission, SPT's final RPI-X control ended in March 2013. SPT was fast-tracked in its RIIO process and the agreed RIIO controls started in April 2013. The distribution controls for the group's networks in the South of Scotland and the Manweb area were reset under RPI-X in April 2010 (Distribution Price Control Review 5) and their review within the RIIO framework is now under way, with a new control due to come into effect in April 2015.

UK ELECTRICITY AND GAS INDUSTRY REGULATION *continued*

Other issues

Other key elements of the regulatory regime in Great Britain include:

Electricity Market Reform ("EMR")

The UK Government continued to develop its proposals for EMR, aimed at providing a framework for the necessary investment for decarbonisation of Britain's energy supply while maintaining security of supply and an acceptable level of costs. The elements of the proposals are:

- a new incentive scheme, based on feed-in tariffs and contracts for difference to support low carbon generation, with the Renewables Obligation ("RO") preserved for plants commissioning until April 2017;
- a market-wide capacity mechanism to support security of supply;
- an emission performance standard, to control the construction of high carbon plant; and
- carbon price support – a tax designed to raise the price of carbon for UK generators.

Carbon price support is already legislated: the UK Treasury tax on fossil fuels used for electricity generation took effect 1 April 2013. The effect of this will be that UK power generators face a higher effective carbon price than specified under the European Union Emissions Trading Scheme ("EU-ETS"). For the year starting 1 April 2013, the uplift will be £4.94/tonne CO₂, rising to £9.55 from 1 April 2014 and £18.08 from 1 April 2015. It is intended that the combination of this tax and the EU-ETS price will rise on a trajectory up to £30/tonne in 2009 prices by 2020.

The remainder of EMR is the main subject for the latest Energy Bill, which has been approved by the House of Commons and moved to the House of Lords in June 2013. The Bill also includes powers to set a carbon intensity target for the electricity sector, provisions (mentioned above) relating to the Retail Market Review, a new enforcement power for Ofgem to require energy businesses that breach licence conditions to provide redress to consumers who suffer detriment as a result of the breach, provisions allowing the Secretary of State to set specific objectives for Ofgem, and provisions to set up an independent Office of Nuclear Regulation.

The Renewables Obligation

The UK Government intends to source around 30 per cent of electricity from renewable sources by 2020 and the RO, introduced in 2002, is currently the main support scheme for renewable electricity projects in support of this aim. The RO Orders (which apply separately to different parts of the UK within a unified scheme) place obligations on suppliers of electricity to source an increasing proportion of their electricity from renewable sources (based on the higher of specified minimum targets and the expected level of renewable generation in the year plus ten per cent "headroom"). Suppliers meet their obligations by presenting sufficient Renewables Obligation Certificates ("ROCs") and/or paying a set "buy-out" price into a fund.

The proceeds of the fund are paid back to those suppliers that have presented ROCs in proportion to the number of ROCs presented. Since April 2009, the RO has been "banded" so that differing technologies get different levels of support, depending on their expected costs. A review of bandings concluded in 2012, as a result of which new projects commissioning in April 2013 (or later for some technologies) receive revised levels of support.

Projects that started generation before 1 April 2009 receive support until 31 March 2027 and projects that started from 1 April 2009 receive support for 20 years subject to closure of the RO on 31 March 2037. The UK Government has said that the RO will close to new projects on 1 April 2017, to be replaced by the EMR arrangements. It will continue to operate for new facilities joining the RO before that date, but from 1 April 2027 the Energy Bill proposes to change its form to a premium payment.

European Union Emissions Trading Scheme

Like in all EU Member States, generators in the UK participate in the EU-ETS. The Department of Energy and Climate Change has responsibility for administering the National Allocation Plan ("NAP"). So far, the majority of EU Allowances ("EUAs") have been issued as free allowances: the UK Government decided to auction or sell seven per cent of EUAs issued under its Phase II NAP. From 2013, the Government are required to auction all allocations to the power sector. The Climate Change Act 2008 set out a trajectory towards reducing greenhouse gas emissions from 1990 levels by at least 80 per cent by 2050, with interim reduction targets.

Domestic Energy Efficiency schemes

Energy suppliers who supply over 250,000 domestic customers ("obligated suppliers") are subject to significant requirements to achieve energy efficiency improvements among their customers. As with any other cost, the costs of making those improvements (less any money received from the customer directly or through the Green Deal – see below) can be factored by suppliers into tariffs, subject to the need to remain competitive in the market.

The Carbon Emissions Reduction Target ("CERT") and Community Energy Saving Programme ("CESP") schemes ended in December 2012, although Ofgem invited those who were unable to complete their obligations on time to undertake mitigation actions (such as further insulation) in 2013. CERT required obligated suppliers to achieve a specified amount of carbon reduction, benchmarked against eligible measures such as cavity wall insulation, loft insulation and appliance improvements. CESP applied to obligated suppliers and also large generators. It was designed to achieve concentrated energy efficiency upgrades, largely going beyond the normal CERT measures, in very low income areas.

The Energy Company Obligation ("ECO") replaced CERT and CESP and runs from 1 January 2013 to 31 March 2015. It comprises three separate targets: the Home Heating Cost Reduction Obligation, which requires suppliers to deliver insulation and heating systems to vulnerable customers living in privately owned properties; the Carbon Saving Community Obligation, which requires suppliers to provide insulation and energy saving measures to properties in low income areas, including some in rural communities; and the Carbon Emission Reduction Obligation which requires suppliers to deliver solid wall insulation or non-standard cavity wall insulation to any applicable property.

DIRECTORS' REPORT *continued*

UK ELECTRICITY AND GAS INDUSTRY REGULATION *continued*

Green Deal

The Green Deal is a mechanism that allows householders and businesses to receive funding for energy efficiency measures, to be repaid through a surcharge on their electricity bill. Customers have been able to sign up to Green Deal plans from January 2013 with suppliers collecting payments from March 2013. Suppliers are obliged to administer the cash collection arrangements on behalf of Green Deal Providers and may also participate as Providers themselves. Measures are to be designed by accredited providers and must meet the "Golden Rule" that the savings from reduced consumption are projected to exceed the cash repayments. In some cases, this will be achieved by the measure receiving a subsidy through the ECO scheme described above. It is as yet unclear how enthusiastic consumers will be about taking up the Green Deal.

Pollution controls

The Integrated Pollution Prevention and Control, the Large Combustion Plant Directive ("LCPD") and the Industrial Emissions Directive ("IED") cover the regulatory regime for controlling pollution from certain industrial activities, including thermal combustion generation, and impose limits on various categories of emissions. In particular, the LCPD limits the emission of sulphur dioxide, oxides of nitrogen and dust from power stations, whereby operators of such plant had the option of meeting those requirements or accepting a limited hours derogation prior to closure by the end of 2015. The IED puts in place a similar regime for 2016 and beyond, with more stringent standards. The IED is transposed into UK law through the Pollution Prevention and Control (Scotland) Regulations 2012 and amendments to the Environmental Permitting (England and Wales) Regulations 2010.

RESEARCH AND DEVELOPMENT

ScottishPower supports research into development of the generation, transmission, distribution and supply of electricity. It also continues to contribute, on an industry-wide basis, towards the cost of research into electricity utilisation and distribution developments. In support of the Strategic plan, ScottishPower also participates in joint research and development ("R&D") activities across the Iberdrola group. During the year ended 31 December 2012 research and development expenditure charged to the group's profit from operations was £2.7 million.

Further details in relation to ScottishPower's R&D activities can be found via statutory disclosures for the Innovation Funding Incentive and Low Carbon Network Fund. Detailed information in relation to ScottishPower's wider R&D activities can be found in the Iberdrola Innovation Report. The report for 2011-12 can be accessed via the 'Innovation' section of www.iberdrola.com.

ENVIRONMENTAL MANAGEMENT AND REGULATION

Throughout its operations, ScottishPower strives to meet, or exceed, relevant legislative and regulatory environmental requirements and codes of practice. Our businesses have environmental systems in accordance with ISO 14001:2004, including fully accredited systems within the Energy Wholesale and Energy Networks businesses. The environmental activities of ScottishPower are governed within the Iberdrola Global Environmental Management Model.

Detailed information on ScottishPower's approach to environmental management and performance for 2012 can be found in the 'Environment' section of the 'ScottishPower Sustainability Summary' that can be found in the 'Corporate Responsibility' section of www.scottishpower.com or via the Iberdrola Sustainability Report that can be found in the 'Shareholders and Investor's' section of www.iberdrola.com.

A listing of material Environmental Regulations is described further above. Further information on applicable environmental regulations is available on request from the company secretary.

EMPLOYEES

The group had 7,190 employees as at 31 December 2012. Of these, 2,797 were employed in Energy Networks, 754 in Energy Wholesale, 2,685 in Energy Retail and 239 in Renewables, with the remaining employed in corporate services.

Employment regulation

ScottishPower has well-defined policies in place throughout its businesses to ensure compliance with applicable laws and related codes of practice. These policies cover a wide range of employment issues such as disciplinary action, grievance, harassment, discrimination, stress and 'whistle-blowing' and have been brought together in the Code of Ethics of Iberdrola and its group of companies (which also outlines expectations for employees' conduct). Further policies and measures were introduced in 2011 to ensure the group complies with the Bribery Act 2010.

Employee consultation

Regular consultation takes place on key business initiatives of issues raised by employees using a variety of means, including monthly team meetings, team managers' conferences, business unit road shows, safety committees, presentations and employee magazines. The group believes that an important element of a positive working experience is stable employee and industrial relations; it recognises the legitimacy of trade union involvement and has formal agreements in place to foster open, two-way communication and consultation. Positive relationships and ongoing liaison with employees and their representatives are seen as contributing significantly to achieving the performance objectives of the businesses.

Equal opportunities

ScottishPower is committed to equal opportunities for all, irrespective of age, disability, gender reassignment, race, religion or belief, sex, sexual orientation, marriage and civil partnership, pregnancy and maternity or other considerations that do not affect a person's ability to perform their job. Further details of group workplace policy and performance can be found in the 'Corporate Responsibility' section of www.scottishpower.com.

DIRECTORS' REPORT *continued*

EMPLOYEES *continued*

Employment of disabled persons

In support of the Policy on Equal Opportunities (above), ScottishPower expects all employees to be treated with respect and has a Policy on People with Disabilities to help ensure equality of employment opportunity for people with disabilities. The aim of the policy is to establish working conditions which encourage the full participation of people with disabilities, which may be achieved through activities such as: making adjustments and/or adaptations to premises; enabling access to the full range of recruitment and career opportunities including the provision of specialist training; and the retention of existing staff who are affected by disability, through rehabilitation, training and reassignment. ScottishPower also works with support organisations, such as Business Disability Forum, which provide support, guidance and sharing of best practice to enable companies to become disability confident.

Positive about disabled people - Double tick accreditation

ScottishPower is a disability positive organisation and in February 2011 was re-accredited and retained the double tick symbol, which recognises the positive action and good practices the organisation has continuously adopted to ensure the required commitments to good employment practice specified by Jobcentre Plus are being met in areas such as recruitment and selection, career development, consultation, retention and redeployment of disabled people.

HEALTH AND SAFETY

The prevention of harm to employees, contractors and members of the public, and the protection of business assets and operational capability is a top priority for ScottishPower. The organisation has continued to strive for improved performance and both internal and external assessments have again returned positive findings. The main business areas within ScottishPower maintained OHSAS 18001 Health and Safety Management System accreditation. The annual ScottishPower employee accident and incident statistics have remained positive during 2012, however there have been ten employee lost time accidents reported to the Health and Safety Executive ("HSE") under The Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 1995 ("RIDDOR"), against thirteen under RIDDOR for the previous year. The commitment to investigate accidents and incidents to address root causes remains steadfast and is given the highest priority with panels of inquiry being established whenever there is a significant incident.

ScottishPower has developed a leading approach to Process Safety and the management of its Generation assets incorporating coal, gas and hydro-electric power stations. At the heart of these operations is a real-time Process Safety dashboard incorporating leading and lagging indicators. These indicators display the health of the risk control carriers whose integrity is closely monitored. Working with our partner, the AMOR Group, ScottishPower has developed a commercial Process Safety product that has been bought by a number of companies internationally.

Provision of public safety information and education about electricity safety has continued through delivery of a mixture of internet, community and school teaching programmes. 'Power Wise' is a safety education programme teaching primary school children aged four to eleven years the potential dangers of electricity in the home and outdoors environment. The programme is curriculum linked and taught by qualified school teachers in primary schools across our operating areas in Scotland, England and Wales. 'Power Wise' was awarded a Business in the Community Big Tick Re-accreditation in the Education category at the National Awards for Excellence 2012. The award was presented by HRH The Prince Charles, Duke of Rothesay, at a prestigious event in Edinburgh.

As well as delivering safety education in schools, ScottishPower provides electrical safety information advice to groups that are at a high risk of coming into contact with apparatus on the electricity network, including agricultural and construction workers.

ScottishPower's Occupational Health Department provide a programme of comprehensive health surveillance and monitoring to "at risk" employee groups to give assurance that control measures intended to prevent work-related diseases remain effective. All potential employees and those employees with medical disability are assessed to ensure productive and safe working arrangements are in place. ScottishPower employment policies provide flexible working arrangements for employees with dependent care and other personal needs. Employee wellbeing continues to be a focus and our people are encouraged to participate in a number of wellbeing events and challenges throughout the year. The promotion of employee wellbeing was further acknowledged by the retention of Scotland's Healthy Working Lives Gold Award.

COMMUNITY RELATIONSHIPS

Community relationships

Building the trust of communities has been part of ScottishPower's core values for many years. The organisation has a long track record of supporting communities not only financially, but also by sharing its resources and the skills of its employees. ScottishPower promotes payroll giving and encourages employee development through community based programmes.

The Fundación Iberdrola is responsible for coordinating, driving and promoting the social and environmental activities of the Iberdrola group. ScottishPower's community investment activity is aligned to the Fundación's four key themes: Training & Research, Sustainability & Biodiversity, Art & Culture and Cooperation and Solidarity.

ScottishPower engages with communities across its operations, particularly where new developments are planned, to ensure community groups can have a say in the planning process.

Community consultation

The key areas where ScottishPower's business impacts upon the community include the siting of new facilities, the presence of distribution and transmission lines and routine maintenance and upkeep work.

A variety of methods of consultation are used to keep in touch with the needs and concerns of the communities potentially affected. ScottishPower's community consultation processes include representation at community meetings, presentations and forums. ScottishPower's power stations host visits from community groups, maintain a number of visitor centres and run Local Liaison Committees which provide a forum for discussion between local management teams and community representatives.

Many of ScottishPower's assets, such as pylons, are on land not owned by ScottishPower, so it is important that effective policies are in place to ensure that the safety and integrity of the plant is maintained, while respecting the needs of the landowner and local community.

Investing in the community

ScottishPower uses the London Benchmarking Group ("LBG") model to evaluate its community investment activity. The model is used by hundreds of leading businesses around the world and provides a comprehensive and consistent set of measures for companies to determine their contributions to the community.

During the year ended 31 December 2012, ScottishPower's businesses contributed £6.2 million in community support activity of which £3.9 million was contributed to registered charitable organisations. The £6.2 million total incorporated £1.8 million categorised as charitable gifts, £2.8 million categorised as community investment and £1.6 million categorised as commercial initiatives, given in cash, through staff time and in-kind donations.

These figures are compiled from ScottishPower's Community Database, which provides an analysis of community investment activity, which is submitted annually in a return to the LBG. The figures provided above will form part of the company's 2013 return and have not yet been audited by LBG.

Further details of ScottishPower's community investment activity and performance can be found in the 'Corporate Responsibility' section of www.scottishpower.com.

DIRECTORS' REPORT *continued*

CORPORATE GOVERNANCE

The ultimate parent of the company is Iberdrola S.A., which is listed on the Madrid stock exchange.

As a general guiding principle, the group adopts the principles and rules contained in the most widely recognised good governance recommendations and, in particular, has taken as a reference the Uniform Good Governance Code for Listed Companies approved by the National Securities Market Commission of Spain.

Administrative, management and supervisory bodies

Board and management meetings

The company is governed by a Board, consisting of three directors who bring a broad range of skills and experience to the company. All are full-time employees of the Iberdrola group.

The directors of the company are subject to annual evaluation of their performance in respect of their executive responsibilities as part of the performance management system which is in place throughout ScottishPower.

The Co-ordination Committee ensures executive focus on co-ordinating the activities of ScottishPower.

The Co-ordination Committee meets fortnightly and receives regular information on the activities of ScottishPower in order to support the corporate functions and lines of business in understanding the local, legal, regulatory and market specifics in the UK and assist the Chief Corporate Officer ("CCO") in the performance of his duties. The Co-ordination Committee reports to the ScottishPower Board and currently comprises the following executives: the CCO, directors of Finance, Regulation, Human Resources ("HR"), Communications, the Chief Executive Officer ("CEO") of the Liberalised Business, the CEO of the Regulated Business, the CEO of the Renewables Business and the Head of Legal.

The Boards of SPENH, SPGH and SPREL are responsible for the effective management of the Regulated (Energy Networks), Liberalised (Energy Wholesale and Energy Retail) and Renewables businesses respectively, in accordance with the strategy set by the ScottishPower Board. These Boards meet regularly and review strategy, operational performance and risk issues on behalf of the respective business.

SPENH Board

The SPENH Board comprises the Chairman Javier Villalba Sanchez and six other directors. The directors and their attendance at SPENH Board meetings held during the period under review (five meetings) are shown in the table below:

Javier Villalba Sanchez (Chairman)	Attended all meetings
Frank Mitchell (Chief Executive Officer)	Attended all meetings
Nicola Connelly	Attended all meetings
Antonio Espinosa de los Monteros	Attended all meetings
José Izaguirre Nazar	Attended all meetings
Scott Mathieson	Attended all meetings
Dame Denise Holt (Independent non-executive director appointed 24 May 2012)	Attended three meetings

SPGH Board

The SPGH Board comprises the Chairman Francisco Martínez Córcoles and seven other directors. The directors and their attendance at SPGH Board meetings held during the period under review (four meetings) are shown in the table below:

Francisco Martínez Córcoles (Chairman)	Attended all meetings
Neil Clitheroe (Chief Executive Officer)	Attended all meetings
Heather Chalmers	Attended all meetings
Ángel Chiarri Toscano	Attended all meetings
Hugh Finlay	Attended all meetings
Oscar Fortis Pita	Attended all meetings
Aitor Moso Raigoso	Attended all meetings
Félix Rojo Sevillano	Attended three meetings
Fernando Tallón Yáñez (resigned 9 April 2012)	Attended one meeting

DIRECTORS' REPORT *continued*

CORPORATE GOVERNANCE *continued*

SPREL Board

The SPREL Boards comprises the Chairman Xabier Viteri and four other directors. The directors and their attendance at SPREL board meetings held during the period under review (four meetings) are shown in the table below:

Xabier Viteri (Chairman)	Attended all meetings
Keith Anderson (Chief Executive Officer)	Attended all meetings
Jonathan Cole (appointed 30 May 2012)	Attended two meetings
Pablo Canales Abaitua	Attended three meetings
Javier Garcia de Fuentes (appointed 30 May 2012)	Attended three meetings
Dame Denise Holt (resigned 4 May 2012)	Attended one meeting
Professor Susan Deacon (resigned 30 May 2012)	Attended two meetings
Regina Reyes Gallur (resigned 29 May 2012)	Attended one meeting

Non-executive oversight is provided at ScottishPower group level by the ScottishPower Board.

ScottishPower Board

The ScottishPower Board comprises the Chairman José Ignacio Sánchez Galán and eight other directors. José Ignacio Sánchez Galán is also the Chairman and Chief Executive of Iberdrola.

The directors of Scottish Power Limited and their classifications are shown in the table below:

José Ignacio Sánchez Galán	Chairman, non-independent, non-executive director
Lord Kerr of Kinlochard GCMG	Independent non-executive director (appointed Vice Chairman 18 April 2012)
José Miguel Alcolea Cantos	Non-independent, non-executive director
Keith Anderson	Executive director (appointed 4 January 2012)
Fernando Becker Zuazua	Non-independent, non-executive director (resigned 31 May 2012)
Professor Susan Deacon	Independent non-executive director (appointed 18 July 2012)
Sir Tom Farmer CVO CBE KCSG	Independent non-executive director
Rt Hon Lord Macdonald of Tradeston CBE	Independent non-executive director
Amparo Moraleda Martinez	Non-independent, non-executive director (resigned 31 January 2012)
Juan Carlos Rebollo Liceaga	Non-independent, non-executive director
José Sainz Armada	Non-independent, non-executive director
José Luís San Pedro Gerenabarrena	Non-independent, non-executive director (resigned 31 May 2012)

ScottishPower Board meetings were held on five occasions during the period under review. Attendance by the directors was as follows:

José Ignacio Sánchez Galán	Attended all meetings
Lord Kerr of Kinlochard GCMG	Attended all meetings
José Miguel Alcolea Cantos	Attended all meetings
Keith Anderson	Attended all meeting
Fernando Becker Zuazua (resigned 31 May 2012)	Attended no meetings
Professor Susan Deacon (appointed 18 July 2012)	Attended three meetings
Sir Tom Farmer CVO CBE KCSG	Attended three meetings
Rt Hon Lord Macdonald of Tradeston CBE	Attended all meetings
Amparo Moraleda Martinez (resigned 31 January 2012)	Attended no meetings
Juan Carlos Rebollo Liceaga	Attended all meetings
José Sainz Armada	Attended all meetings
José Luís San Pedro Gerenabarrena (resigned 31 May 2012)	Attended two meetings

There is no designated Senior Independent Director on the ScottishPower Board.

DIRECTORS' REPORT *continued*

CORPORATE GOVERNANCE *continued*

ScottishPower Audit and Compliance Committee ("ACC")

The ACC, a permanent internal body, has an informative and consultative role, without executive functions, with powers of information, assessment and presentation of proposals to the ScottishPower Board within its scope of action, which is governed by the Memorandum and Articles of Association of Scottish Power Limited and by the Terms of Reference of the ACC. The ACC's responsibilities include:

- monitoring the financial reporting process for ScottishPower;
- monitoring the effectiveness of the ScottishPower's internal control, internal audit and risk management systems; and
- monitoring the statutory audit of the annual and consolidated accounts of ScottishPower.

The ACC comprises three members. The Chairman of the ACC has relevant accounting and financial experience, and there is one independent member on the ACC as indicated in the table below.

The ACC met five times during the year under review. The members of the ACC and their attendance record are shown in the table below:

Rt Hon Lord Macdonald of Tradeston CBE (Chairman)	External independent, attended all meetings
Juan Carlos Rebollo Liceaga (Chairman)	Attended all meetings
José Miguel Alcolea Cantos	Attended three meetings (resigned 17 July 2012)
Professor Susan Deacon	External independent, attended two meetings (appointed 17 July 2012)

On 2 February 2012, Juan Carlos Rebollo Liceaga was succeeded as Chairman of the ACC by Rt Hon Lord Macdonald of Tradeston CBE.

Iberdrola Appointments and remuneration ("IARC")

There is no separate Nomination Committee or Remuneration Committee within ScottishPower. Instead nomination and remuneration matters relevant to ScottishPower are dealt with by the IARC. The members of the IARC are:

Inés Macho Stadler (Chairman)	External independent
José Ignacio Berroeta Echevarría (Chairman)	External independent (resigned 24 April 2012)
Iñigo Victor de Oriol Ibarra	External independent
Santiago Martínez Lage	External independent (appointed 24 April 2012)

On 24th April 2012, José Ignacio Berroeta Echevarría was succeeded as Chairman of the IARC by Inés Macho Stadler.

The IARC has the power to supervise the process of selection of directors and senior managers of the Iberdrola group companies, and to assist the Boards of Directors in the determination and supervision of the compensation policy for the above-mentioned persons.

Internal control

During the year under review, the directors of the company had overall responsibility for establishing and maintaining an adequate system of internal controls within the group and they participated in the review of internal controls over financial reporting, the preparation of consolidated Accounts and the certification process which took place on a ScottishPower group-wide basis. The effectiveness of the system within ScottishPower was kept under review through the work of the ACC. The system of internal control is designed to manage rather than eliminate risk. In pursuing these objectives, internal control can only provide reasonable and not absolute assurance against material misstatement or loss.

A risk and control governance framework is in place across ScottishPower. The risk management framework and internal control system is subject to continuous review and development. The company is committed to ensuring that a proper control environment is maintained. There is a commitment to competence and integrity and to the communication of ethical values and control consciousness to managers and employees. HR policies underpin that commitment by a focus on enhancing job skills and promoting high standards of probity among staff. In addition, the appropriate organisational structure has been developed within which to control the businesses and to delegate authority and accountability, having regard to acceptable levels of risk. The company's expectations in this regard are set out in 'ScottishPower Code of Ethics', a policy document which aims to summarise some of the main legal, regulatory, cultural and business standards applicable to all employees. This document has been distributed to all employees of the company.

ScottishPower has fraud and anti-bribery policies and procedures in place to ensure that all incidences of fraud and bribery are appropriately investigated and reported. Further, ScottishPower has adopted a revised Speaking Out and Whistleblower Protection Policy, incorporating a confidential external reporting service operated by an independent provider. This policy, which is applicable to employees of the company, covers the reporting and investigation of suspected fraud, bribery, and misappropriation, questionable accounting, financial reporting or auditing matters, breaches of internal financial control procedures, and serious breaches of behaviour and ethical principles. There is also a process in existence within ScottishPower whereby all members of staff may report any financial irregularities to the Audit, Risk and Supervision Committee of Iberdrola.

DIRECTORS' REPORT *continued*

CORPORATE GOVERNANCE *continued*

Identification and evaluation of risks and control objectives

During the year under review the ScottishPower governance structure was supported by risk policies adopted by the ScottishPower Board. These risk policies are adopted by the ScottishPower Board on an annual basis. ScottishPower business risk assessment teams and the independent group risk management function support the ScottishPower Board in the execution of due diligence and risk management. In addition, the SPENH and SPGH Boards are responsible for ensuring that their respective businesses' risks are adequately assessed, monitored, mitigated and managed.

ScottishPower's strategy, which is adopted by the company, is to conduct business in a manner benefiting customers through balancing cost and risk while delivering shareholder value and protecting ScottishPower's performance and reputation by prudently managing the risks inherent in the business. ScottishPower develops and implements risk management policies and procedures, and promotes a robust control environment at all levels of the organisation.

The company identifies and assesses the key business risks associated with the achievement of its strategic objectives. Any key actions needed to further enhance the control environment are identified, along with the person responsible for the management of the specific risk.

Auditor independence

The Audit, Risk and Supervision Committee of Iberdrola is responsible for the nomination of the external auditors. This committee and the firm of external auditors have safeguards to avoid the possibility that the auditors' objectivity and independence could be compromised.

Where the work to be undertaken is of a nature that is generally considered reasonable to be completed by the external auditors for sound commercial and practical reasons, including confidentiality, the conduct of such work is permissible provided that it has been pre-approved by the ScottishPower Board.

Social, environmental and ethical matters

Social, environmental and ethical ("SEE") matters are managed through the risk management framework and internal control system within the group. As such, regular account is taken of the strategic significance of SEE matters to the group, and the risks and opportunities arising from these issues that may have an impact on the group's short-term and long-term values are considered.

Further information regarding the SEE matters can be found in the 'Corporate Responsibility' section of www.scottishpower.com.

POLITICAL DONATIONS AND EXPENDITURE

The group is a politically neutral organisation. It is subject to the Political Parties, Elections and Referendums Act 2000, which defines political "donations" and "expenditure" in wider terms than would be commonly understood by these phrases. During the year ended 31 December 2012, the group paid a total of £23,000 for the sponsorship of conferences and events – activities which may be regarded as falling within the terms of the Act. The recipients of these payments were:

- | | |
|--------------------------------|--------|
| • The Conservative Party | £7,000 |
| • The Labour Party | £7,000 |
| • The Scottish National Party | £7,000 |
| • Plaid Cymru – Party of Wales | £2,000 |

These occasions provide an important opportunity for the group to represent its views on a non-partisan basis to politicians from across the political spectrum. The payments do not indicate support for any particular party.

CREDITOR PAYMENT POLICY AND PRACTICE

The group's policy and practice is to settle terms of payment when agreeing the terms of the transaction, to include the terms in contracts and to pay in accordance with its contractual and legal obligations. The group's creditor days at 31 December 2012 were 9 days (31 December 2011 5 days).

DIRECTORS

The directors who held office during the year were as follows:

Daniel Alcain Lopez	(appointed 20 August 2012)
Ramón Fernández Olmedo	(resigned 20 August 2012)
Marion Venman	
Donald Wright	

DIRECTORS' REPORT *continued*

DIRECTORS' RESPONSIBILITIES FOR THE ACCOUNTS

The directors are responsible for preparing the Directors' Report and Accounts in accordance with applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

The directors are responsible for preparing Accounts for each financial period which give a true and fair view, in accordance with IFRSs, of the state of affairs of the company and the group and of the profit or loss of the group for that period. In preparing those Accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether the parent company and the group Accounts comply with IFRSs, subject to any material departures disclosed and explained in the Accounts; and
- prepare the Accounts on the going concern basis unless it is inappropriate to presume that the group will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and the group and to enable them to ensure that the parent company Accounts and the group Accounts comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Each of the directors in office as at the date of this Directors' Report and Accounts confirms that:

- so far as he or she is aware, there is no relevant audit information of which the company's auditor is unaware; and
- he or she has taken all the steps that he or she ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that the company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

AUDITORS

Ernst & Young LLP were re-appointed auditors of the company for the year ended 31 December 2012.

BY ORDER OF THE BOARD



Marion Venman

Secretary

25 June 2013

INDEPENDENT AUDITORS' REPORT

to the member of Scottish Power UK plc

We have audited the Accounts of Scottish Power UK plc for the year ended 31 December 2012 which comprise the Consolidated and Company Balance Sheets, the Consolidated Income Statement, the Consolidated and Company Statements of Comprehensive Income, the Consolidated and Company Statements of Changes in Equity, the Consolidated and Company Cash Flow Statements, and the related notes 1 to 54. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's member 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 member those matters we are required to state to it in an auditors' 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 member, as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibilities Statement set out on page 15, the directors are responsible for the preparation of the Accounts and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Accounts in accordance with the applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE ACCOUNTS

An audit involves obtaining evidence about the amounts and disclosures in the Accounts sufficient to give reasonable assurance that the Accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the Accounts. In addition, we read all the financial and non-financial information in the Directors' Report and Accounts to identify material inconsistencies with the audited accounts. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON ACCOUNTS

In our opinion:

- the Accounts give a true and fair view of the state of the group's and the parent company's affairs as at 31 December 2012 and of the group's profit for the year then ended;
- the group Accounts have been properly prepared in accordance with IFRS's as adopted by the European Union;
- the parent company Accounts have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the Accounts have been prepared in accordance with the requirements of the Companies Act 2006.

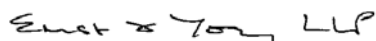
OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006

In our opinion the information given in the Director's Report for the financial year for which the Accounts are prepared is consistent with the Accounts.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company Accounts 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.



James Nisbet (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Glasgow
25 June 2013

SCOTTISH POWER UK PLC AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

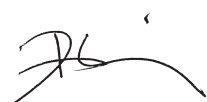
at 31 December 2012 and 31 December 2011

	Notes	2012 £m	2011 £m
ASSETS			
NON-CURRENT ASSETS			
Intangible assets		1,193.5	307.4
Goodwill	7	446.7	82.1
Other intangible assets	7	746.8	225.3
Property, plant and equipment		8,999.1	6,454.3
Property, plant and equipment in use	8	7,870.4	5,388.2
Property, plant and equipment in the course of construction	8	1,128.7	1,066.1
Financial assets		125.6	226.0
Investments accounted for using the equity method		2.4	2.6
Other investments	9	1.8	1.1
Finance lease receivables	9	2.2	2.4
Derivative financial instruments	9, 19	119.2	219.9
Trade and other receivables	11	4.9	–
NON-CURRENT ASSETS		10,323.1	6,987.7
CURRENT ASSETS			
Inventories	10	110.6	228.7
Trade and other receivables	11	3,120.1	2,266.7
Financial assets		248.4	350.9
Finance lease receivables	9	0.2	0.2
Derivative financial instruments	9, 19	217.4	332.0
Cash and cash equivalents and term deposits	9	30.8	18.7
CURRENT ASSETS		3,479.1	2,846.3
TOTAL ASSETS		13,802.2	9,834.0

SCOTTISH POWER UK PLC AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS *continued*
at 31 December 2012 and 31 December 2011

	Notes	2012 £m	2011 £m
EQUITY AND LIABILITIES			
EQUITY			
Equity of shareholders of the parent	13	3,778.3	2,085.6
Share capital	12, 13	872.0	872.0
Share premium	13	398.2	398.2
Hedge reserve	13	(109.1)	(72.6)
Other reserves	13	14.0	14.0
Retained earnings	13	2,603.2	874.0
Of non-controlling interests	14	0.2	–
TOTAL EQUITY		3,778.5	2,085.6
NON-CURRENT LIABILITIES			
Deferred income	15	804.1	728.7
Provisions		615.7	299.5
Provisions for retirement benefit obligations	16	498.7	212.1
Other provisions	17	117.0	87.4
Bank borrowings and other financial liabilities		2,389.6	2,010.4
Loans and other borrowings	18	2,328.8	1,884.3
Derivative financial instruments	9, 19	60.8	126.1
Trade and other payables	21	6.1	4.9
Deferred tax liabilities	22	800.4	525.5
NON-CURRENT LIABILITIES		4,615.9	3,569.0
CURRENT LIABILITIES			
Provisions	17	138.3	196.3
Bank borrowings and other financial liabilities		3,694.8	2,436.6
Loans and other borrowings	18	3,397.8	2,048.9
Derivative financial instruments	9, 19	297.0	387.7
Trade and other payables	21	1,459.4	1,494.7
Current tax liabilities		115.3	51.8
CURRENT LIABILITIES		5,407.8	4,179.4
TOTAL LIABILITIES		10,023.7	7,748.4
TOTAL EQUITY AND LIABILITIES		13,802.2	9,834.0

Approved by the Board on 25 June 2013 and signed on its behalf by:



Daniel Alcain Lopez
Director

SCOTTISH POWER UK PLC AND SUBSIDIARIES
CONSOLIDATED INCOME STATEMENTS
for the years ended 31 December 2012 and 31 December 2011

	Notes	2012 £m	2011 £m
Revenue	6	7,803.1	6,440.9
Procurements		(5,770.9)	(5,017.2)
		2,032.2	1,423.7
Staff costs	23	(376.3)	(357.8)
Capitalised staff costs	23	122.2	105.5
Outside services		(410.0)	(342.3)
Other operating income		206.9	254.4
		(457.2)	(340.2)
Taxes other than income tax	24	(287.3)	(170.0)
		1,287.7	913.5
Depreciation and amortisation charge, allowances and provisions	25	(434.6)	(544.0)
PROFIT FROM OPERATIONS		853.1	369.5
Result of companies accounted for using the equity method		–	–
Gains on disposal of non-current assets		4.4	0.3
Losses on disposal of non-current assets		(0.5)	(0.1)
Finance income	26	190.9	184.2
Finance costs	27	(306.2)	(259.1)
PROFIT BEFORE TAX		741.7	294.8
Income tax	28	(93.5)	(27.5)
NET PROFIT FOR THE YEAR		648.2	267.3
Non-controlling interests	14	(0.1)	–
NET PROFIT FOR THE YEAR ATTRIBUTABLE TO THE PARENT		648.1	267.3

All results relate to continuing operations.

SCOTTISH POWER UK PLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

for the years ended 31 December 2012 and 31 December 2011

	Note	2012 £m	2011 £m
NET PROFIT FOR THE YEAR		648.2	267.3
OTHER COMPREHENSIVE INCOME			
Cash flow hedges:			
Change in the value of cash flow hedges	13	(11.6)	(87.4)
Tax on items relating to cash flow hedges	13	0.2	21.9
		(11.4)	(65.5)
Actuarial losses on retirement benefits:			
Actuarial losses on retirement benefits	13	(351.7)	(112.2)
Tax relating to actuarial losses on retirement benefits	13	74.0	23.4
		(277.7)	(88.8)
OTHER COMPREHENSIVE INCOME FOR THE YEAR		(289.1)	(154.3)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		359.1	113.0
Total comprehensive income attributable to equity holders of the parent		359.0	113.0
Total comprehensive income attributable to non-controlling interests		0.1	–
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		359.1	113.0

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

for the years ended 31 December 2012 and 31 December 2011

	Attributable to equity holders of the parent						Non-controlling interests £m	Total equity £m
	Ordinary share capital £m	Share premium £m	Hedge reserve £m	Other reserves £m	Retained earnings £m	Total £m		
At 1 January 2011	872.0	398.2	0.8	14.0	777.7	2,062.7	–	2,062.7
Total comprehensive income for the year	–	–	(65.5)	–	178.5	113.0	–	113.0
Business combinations (net of tax)	–	–	(7.9)	–	117.8	109.9	–	109.9
Dividends	–	–	–	–	(200.0)	(200.0)	–	(200.0)
At 1 January 2012*	872.0	398.2	(72.6)	14.0	874.0	2,085.6	–	2,085.6
Total comprehensive income for the year	–	–	(11.4)	–	370.4	359.0	0.1	359.1
Business combinations (net of tax)	–	–	(25.1)	–	1,358.8	1,333.7	0.3	1,334.0
Dividends	–	–	–	–	–	–	(0.2)	(0.2)
At 31 December 2012	872.0	398.2	(109.1)	14.0	2,603.2	3,778.3	0.2	3,778.5

The accompanying Notes 1 to 36 are an integral part of the consolidated statements of comprehensive income and the consolidated statements of changes in equity for the years ended 31 December 2012 and 31 December 2011.

SCOTTISH POWER UK PLC AND SUBSIDIARIES
CONSOLIDATED CASH FLOW STATEMENTS
for the years ended 31 December 2012 and 31 December 2011

	2012 £m	2011 £m
Cash flows from operating activities		
Profit before tax	741.7	294.8
Adjustments for:		
Depreciation, amortisation and impairment	410.9	479.1
Change in provisions	75.5	129.7
Capital grants and transfers of assets from customers	(24.5)	(32.2)
Finance income and costs	115.3	74.9
Net losses on disposal/write-off non-current assets	1.8	6.3
Movement in retirement benefits	(31.7)	(44.6)
Net fair value losses on operating derivatives	4.6	78.4
Movement in deferred income	(58.8)	(116.2)
Movement in plant maintenance stock	(2.5)	1.4
Changes in working capital:		
Change in trade and other receivables	120.0	349.5
Change in inventories	106.4	(19.4)
Change in trade and other payables	(124.1)	(218.8)
Provisions paid	(15.7)	(14.2)
Emission allowances acquired	(3.8)	(27.2)
Assets received from customers	100.4	75.8
Income taxes paid	(51.5)	(101.2)
Interest received	17.4	47.6
Dividends received	–	0.4
Net cash flows from operating activities (i)	1,381.4	964.1
Cash flows from investing activities		
Investments in intangible assets	(155.7)	(12.4)
Investments in property, plant and equipment	(985.9)	(577.4)
Deferred income relating to assets	–	5.0
Proceeds from disposal of available-for-sale investments	–	9.4
Proceeds from disposal of intangibles	–	0.1
Proceeds from disposal of property, plant and equipment	9.6	0.4
Acquisition of subsidiaries	(27.8)	(65.3)
Net cash and cash equivalents acquired	(832.2)	(568.3)
Net cash flows from investing activities (ii)	(1,992.0)	(1,208.5)
Cash flows from financing activities		
Decrease in amounts due from Iberdrola group companies	30.2	–
Dividends paid to company's equity holders	–	(200.0)
Dividends paid to non-controlling interests	(0.2)	–
Cash inflows from borrowings	345.5	363.6
Interest paid	(158.7)	(126.2)
Repayments of borrowings	(9.3)	(287.8)
Net cash flows from financing activities (iii)	207.5	(250.4)
Net decrease in cash and cash equivalents (i)+(ii)+(iii)	(403.1)	(494.8)
Cash and cash equivalents at beginning of year	(689.0)	(194.2)
Cash and cash equivalents at end of year	(1,092.1)	(689.0)
Cash and cash equivalents at end of year comprises:		
Consolidated balance sheet cash and cash equivalents and term deposits	30.8	18.7
Bank overdraft	(0.1)	(0.7)
Receivables due from Iberdrola group companies – loans	2,238.6	1,295.8
Payables due to Iberdrola group companies – loans	(3,361.4)	(2,002.8)
Consolidated cash flow statement cash and cash equivalents	(1,092.1)	(689.0)

The accompanying Notes 1 to 36 are an integral part of the consolidated cash flow statements for the years ended 31 December 2012 and 31 December 2011.

NOTES TO THE CONSOLIDATED ACCOUNTS

31 December 2012

1 GROUP ACTIVITIES

The group provides electricity transmission and distribution services in the UK, supplies gas and electricity services to homes and businesses across the UK, and operates electricity generation, gas storage facilities and associated energy management activities in the UK. Since 1 January 2012, following the acquisition of SPREL, the group has also conducted renewable energy activities across the UK and Republic of Ireland.

The group defines operating segments for management purposes based on a combination of factors, principally differences in products and services and the regulatory environment in which each business operates.

For management purposes, the group was organised into four operating segments during the year, Energy Networks, Energy Wholesale, Energy Retail and Renewables.

Energy Networks

The transmission and distribution businesses within the group's authorised area of Scotland and the distribution business of Manweb operating in Merseyside, Cheshire and North Wales.

Energy Wholesale

The generation of electricity from the group's own power stations, the purchase of external supplies of coal and gas for the generation of electricity, the purchase of external supplies of electricity and gas for onward sale to customers, gas storage and the sale of electricity to market participants in the UK, and full participation in the British Electricity Trading and Transmission Arrangements ("BETTA").

Energy Retail

The sale of electricity and gas to industrial and domestic customers, together with related billing and collection activities and the group's energy services activity.

Renewables

The construction and development of renewable energy generation assets and the generation and sale of electricity from these assets.

2 BASIS OF PREPARATION

A. BASIS OF PREPARATION OF THE ACCOUNTS

The company is required by law to prepare accounts for both the company and the group and to deliver them to the Registrar of Companies. Both the group (being these consolidated Accounts) and the company's individual Accounts, have been prepared in accordance with International Accounting Standards ("IAS"), International Financial Reporting Standards ("IFRSs") and International Finance Reporting Interpretations Committee ("IFRIC") Interpretations (collectively referred to as IFRS), as adopted by the EU as at the date of approval of these Accounts and which are mandatory for the financial year ended 31 December 2012. Both the group and company Accounts are prepared in accordance with the Accounting Policies set out in Note 3.

B. BASIS OF CONSOLIDATION

The consolidated Accounts incorporate the Accounts of the company and its subsidiaries to 31 December each year.

Subsidiaries are those entities over which the group has the power to govern the financial and operating policies, generally accompanying a shareholding that confers more than half of the voting rights.

On acquisition, the assets and liabilities of a subsidiary are measured at their fair values at the date of acquisition. The cost of an acquisition is measured at the fair value of any assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. The interest of minority shareholders is initially stated at the minority's proportion of the fair values of the assets and liabilities recognised. In accordance with the exemption permitted by IFRS 1 'First-time Adoption of International Financial Reporting Standards', business combinations accounted for prior to the group's date of transition to IFRS on 1 April 2004 have not been restated to comply with IFRS 3 'Business Combinations'.

The results of subsidiaries acquired or disposed of during the year are included in the income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

For the consolidated group, intra-group transfers of subsidiaries within the Iberdrola group, but outwith Scottish Power UK plc group, are deemed to be business combinations under common control. These transactions are accounted for using the pooling of interests method. The results for the subsidiaries transferred are included in the income statement from the effective date of acquisition. The net assets incorporated at the date of acquisition reflect the book value of each of the subsidiaries included in the Iberdrola S.A. Consolidated Financial Statements, the highest entity that has common control for which consolidated IFRS financial statements are prepared.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

3 ACCOUNTING POLICIES

The principal accounting policies applied in preparing the group's consolidated Accounts and, where applicable, the company's Accounts are set out below. The 'group' is defined as Scottish Power UK plc and its consolidated subsidiaries. The 'company' or 'SPUK' refers to Scottish Power UK plc.

- A. REVENUE
- B. GOODWILL
- C. INTANGIBLE ASSETS (EXCLUDING GOODWILL)
- D. PROPERTY, PLANT AND EQUIPMENT
- E. LEASED ASSETS
- F. IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS (EXCLUDING GOODWILL)
- G. FINANCIAL INSTRUMENTS
- H. INVENTORIES
- I. GRANTS AND TRANSFERS OF ASSETS FROM CUSTOMERS
- J. RETIREMENT BENEFITS
- K. DECOMMISSIONING COSTS
- L. FOREIGN CURRENCIES
- M. TAXATION
- N. INVESTMENTS

A. REVENUE

Revenue comprises the sales value of electricity and gas and other related energy services supplied to customers during the year and excludes Value Added Tax and intra-group sales. The group recognises revenue in respect of its principal revenue-generating operations as follows:

Transmission and distribution – revenue comprises charges made to the Great Britain system operator for the use of the transmission network and charges made to retailers and customers for use of the distribution network. Revenue includes accruals in respect of unbilled income relating to units transferred over the network established from data flows.

Generation – revenue comprises the value of units supplied during the year. Units are based on energy volumes that can actually be sold on the wholesale market and are recorded on wind farm and power station meters and industry-wide trading and settlement systems. Revenue from wind farms also includes the value of ROCs and Levy Exemption Certificates ("LECs") sold during the year.

Wholesale – revenue comprises value of units of wholesale energy supplied to customers during the year. Units are based on energy volumes that can actually be sold on the wholesale market and are recorded using industry-wide trading and settlement systems. Purchases of wholesale energy are reported within procurements.

Retail – revenue from the sale of energy to retail customers is the value of units supplied during the year and includes an estimate of the value of units supplied to customers between the date of their last meter reading and the year end, based on external data supplied by the electricity and gas market settlement process.

Interest income is accrued on a time proportional basis, by reference to the principal outstanding and the effective interest rate applicable, which is the rate which exactly discounts estimated future cash receipts through the expected life of the asset to that asset's carrying amount.

B. GOODWILL

Goodwill represents the excess of the fair value of the purchase consideration over the group's share of the fair value of the identifiable assets and liabilities of an acquired subsidiary or business at the date of acquisition.

Goodwill is recognised as an asset and reviewed for impairment at least annually and whenever there is an indication of impairment. Any impairment is recognised in the income statement in the period in which it is identified.

On disposal of a subsidiary, associate, jointly controlled entity or business, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Goodwill arising on acquisitions after 31 March 1998 but prior to the group's date of transition to IFRS, 1 April 2004, has been retained as an asset at the previous UK Generally Accepted Accounting Principles amounts as at 1 April 2004.

Goodwill arising on acquisitions prior to 1 April 1998 was written off against reserves and will not be included in determining any subsequent profit or loss on disposal.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

3 ACCOUNTING POLICIES *continued*

C. INTANGIBLE ASSETS (EXCLUDING GOODWILL)

C1. COMPUTER SOFTWARE COSTS

The costs of acquired computer software are capitalised on the basis of the costs incurred to acquire and bring to use the specific software and are amortised on a straight-line basis over their operational lives. Costs directly associated with the development of computer software programmes that will probably generate economic benefits over a period in excess of one year are capitalised and amortised, on a straight-line basis, over their estimated operational lives. Costs include employee costs relating to software development and an appropriate proportion of relevant overheads directly attributable to bringing the software into use. Amortisation of computer software costs is over periods of up to nine years.

C2. EMISSIONS ALLOWANCES

The group participates in the EU Emissions Trading Scheme.

Purchased emissions allowances are initially recognised at cost within intangible assets. Allocated allowances awarded to the group by the government or a similar body are recorded initially at the fair value with a corresponding credit to deferred income, which is released to the consolidated income statement in line with the group's expected emissions over the period covered by the allowances.

The group recognises liabilities in respect of its obligations to deliver emissions allowances at the value at which these allowances were initially recognised on the balance sheet. If it is estimated that it will be necessary to deliver more emission allowances than recorded on the balance sheet, the liability for this shortfall is calculated based on the market price of the allowances at the balance sheet date.

The allowances held within intangible assets may be surrendered at the end of each compliance period reflecting the consumption of economic benefit. As a result no amortisation is recorded during the year.

D. PROPERTY, PLANT AND EQUIPMENT

Group and company property, plant and equipment is stated at cost and is generally depreciated on the straight-line method over the estimated operational lives of the assets. Property, plant and equipment includes capitalised employee, interest and other directly attributable costs. Borrowing costs directly attributable to the acquisition, construction or production of major qualifying assets, which are assets 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. Reviews are undertaken annually of the estimated remaining lives and residual values of property, plant and equipment. Residual values are assessed based on prices prevailing at each balance sheet date.

Land is not depreciated. The main depreciation periods used by the group and the company are as set out below.

	Years
Hydro-electric plants	5-100
Fossil fuel plants	2-50
Combined cycle plants	2-35
Gas storage facilities	10-35
Wind farms	24
Transmission facilities	40-60
Distribution facilities	35-60
Meters and measuring devices	2-10
Other facilities and other items of property, plant and equipment	1-50

E. LEASED ASSETS

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date, whether fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset, even if that right is not explicitly specified in the arrangement. For arrangements entered into prior to 1 April 2004, the date of inception is deemed to be 1 April 2004 in accordance with the transitional requirements of IFRIC 4 'Determining Whether an Arrangement Contains a Lease'.

The group classifies leases as finance leases whenever the lessor transfers substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Finance lease receivables are initially recognised at the lower of the fair value of the leased asset and the present value of future payments. Finance income is subsequently recognised over the useful life of the leased asset using the effective interest method.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

F. IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS (EXCLUDING GOODWILL)

At each balance sheet date, the group reviews the carrying amount of its property, plant and equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the group estimates the recoverable amount of the cash generating unit to which the asset belongs.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

3 ACCOUNTING POLICIES *continued*

G. FINANCIAL INSTRUMENTS

This policy is applicable to both the group's consolidated Accounts and the company's individual Accounts.

G1. ACCOUNTING POLICIES UNDER IAS 39

- (a) Financial assets categorised as trade and other receivables are recognised and carried at original invoice amount less an allowance for impairment of doubtful debts. Allowance for doubtful debts has been estimated by management, taking into account future cash flows, based on past experience and assessment of the current economic environment within which the group operates.
- (b) The carrying amount of finance lease receivables is calculated as set out in Note 3E.
- (c) Cash and cash equivalents and term deposits in the balance sheet comprise cash on hand and term deposits which are readily convertible into a known amount of cash without a significant risk of changes in value. In the cash flow statement, cash and cash equivalents exclude term deposits which have a maturity of more than 90 days at the date of acquisition and include bank overdrafts repayable on demand the next business day and the net of current loans receivable and payable from group companies.
- (d) Financial liabilities categorised as trade and other payables are recognised and carried at original invoice amount.
- (e) All interest bearing loans and borrowings are initially recognised at fair value, net of directly attributable transaction costs. Interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method, except where the loan or borrowing is a hedged item in an effective fair value hedging relationship (see G3 Hedge Accounting).
- (f) Other investments are valued at fair value at the balance sheet date except where it is not possible to obtain a fair value for unquoted investments. Revaluation surpluses and deficits are recognised in the statement of comprehensive income.
- (g) The group enters into sale and purchase transactions for gas, electricity, oil and coal in the normal course of its energy business. Most of these contracts are entered into for the purposes of the group's expected business requirements. These 'own use' contracts are outside the scope of IAS 39 'Financial Instruments: Recognition and Measurement' and are accounted for on an accruals basis.

Certain physical commodity purchase and sale contracts are within the scope of IAS 39 because they are net settled or are capable of net settlement. All such contracts are classified as derivative financial instruments in accordance with IAS 39. The group also enters into treasury-related derivatives to manage its financial risk. The group's policies and management with respect to financial risks are discussed in Note 4.

IAS 39 requires all derivatives to be recognised on the balance sheet at fair value. Embedded derivatives in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not carried at fair value through the income statement.

Unrealised gains or losses on remeasurement of derivatives and embedded derivatives are reported in the income statement except when hedge accounting is applied (see G3 below). Fair value gains and losses on derivatives used in the group's energy management activities are recognised in the income statement within procurements and fair value gains and losses on derivatives used in the group's treasury activities are recognised in the income statement as finance income or finance costs as appropriate.

G2. RISK CONTROL ENVIRONMENT

The group's strategy is to conduct business in a manner benefiting customers through balancing cost and risk while delivering shareholder value and protecting the group's performance and reputation by prudently managing the risks inherent in the business. To maintain this strategic direction the group develops and implements risk management policies and procedures, and promotes a rigid control environment at all levels of the organisation. Further details of the group's strategy and management of risks are discussed in detail in Note 4.

G3. HEDGE ACCOUNTING

Hedge accounting is applied when certain conditions required by IAS 39 are met. Hedge accounting falls into the following categories:

G3.1 CASH FLOW HEDGES

The portion of gain or loss of the hedging instrument that was determined to be an effective hedge is recognised directly in equity and forms part of the hedge reserve. The ineffective portion of the change in fair value of the hedging instruments is recognised in the income statement within procurements for hedges of underlying operations. For hedges of financing activities, any ineffectiveness is recognised within finance income or finance costs, as appropriate, in the income statement. If the cash flow hedge relates to an underlying transaction which results in the recognition of a non-financial asset, the associated gains or losses on the derivative that had previously been recognised in equity are recognised in the initial measurement of the asset arising from the hedged transaction. For hedges that relate to an underlying transaction which results in recognition of a financial asset or a liability, amounts deferred in equity are recognised in the income statement in the same period in which the hedged item affects the income statement.

G3.2 FAIR VALUE HEDGES

The gain or loss from remeasuring the hedging instrument at fair value is recognised directly in the income statement in the same location as the gain or loss from remeasuring the hedged item. The gain or loss on the hedged item adjusts the carrying amount of the hedged item (when the item would otherwise have been measured at amortised cost) and is recognised in the income statement. The group starts amortisation of any such adjustments to the carrying value of the hedged item when the hedging relationship ends.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

3 ACCOUNTING POLICIES *continued*

G. FINANCIAL INSTRUMENTS *continued*

G3.3 HEDGE EFFECTIVENESS

Hedge effectiveness is measured and respective entries recorded in the balance sheet, reserves and income statement on a monthly basis in respect of commodities and on a half-yearly basis in respect of treasury hedging relationships. Hedge effectiveness is achieved where the correlation between the changes in value of the hedging instrument and the hedged item is between 80% and 125%.

G3.4 DISCONTINUING HEDGE ACCOUNTING

The group discontinues prospectively hedge accounting when the hedge instrument expires or is sold, terminated or exercised, when the hedge relationship no longer qualifies for hedge accounting or when the designation is revoked. In the case of cash flow hedging, any gain or loss that has been recognised in equity until that time remains separately recognised in equity until the forecast transaction occurs. If the transaction is no longer expected to occur, related cumulative gains and losses which have been previously deferred in equity are recognised in the income statement.

G4. VALUATION OF FINANCIAL INSTRUMENTS

In those circumstances where IAS 39 requires financial instruments to be recognised in the balance sheet at fair value, the group's valuation strategies for derivative and other financial instruments utilise as far as possible quoted prices in an active trading market.

In the absence of quoted prices for identical or similar assets or liabilities, it is sometimes necessary to apply valuation techniques where contracts are marked using approved models. Models are used for developing both the forward curves and the valuation metrics of the instruments themselves where the instruments are complex combinations of standard or non-standard products. All models are subject to rigorous testing prior to being approved for valuation and subsequent continuous testing and approval procedures designed to ensure the validity and accuracy of the model assumptions and inputs.

G5. OFFSETTING OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The group offsets a financial asset and a financial liability and reports the net amount only when the group has a legally enforceable right to set off the amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

H. INVENTORIES

Inventories are valued at the lower of average cost and net realisable value.

I. GRANTS AND TRANSFERS OF ASSETS FROM CUSTOMERS

Capital and revenue grants and transfers of assets from customers are credited to deferred income within non-current liabilities.

Pursuant to the applicable industry regulations, the group occasionally receives contributions from its customers for the construction of grid connection facilities, or is assigned such assets that must be used to connect those customers to a network and provide them with ongoing access to a supply of goods or services, or both. As the installation received is considered to be payment for ongoing access to the supply of the goods and services, it is credited to deferred income and released to the income statement over the estimated operational lives of the related assets.

Revenue grants and transfers of assets from customers are released to the income statement over the period in which they are intended to contribute to expenditure incurred.

J. RETIREMENT BENEFITS

The group provides pensions through defined benefit schemes and one defined contribution scheme.

The cost of providing benefits under the defined benefit schemes is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are recognised in full, directly in retained earnings, in the period in which they occur and are shown in the statement of comprehensive income. The current service cost element of the pension charge is recognised within 'Staff costs' in the consolidated income statement. The expected return on pension scheme assets and interest on pension scheme liabilities are included within 'Finance income' and 'Finance costs', respectively, in the consolidated income statement. The retirement benefits asset and liability recognised in the balance sheet represent the net surpluses and deficits respectively in the group's defined benefit pension schemes.

Payments to the defined contribution scheme are charged as an expense as they fall due.

K. DECOMMISSIONING COSTS

Provision is made, on a discounted basis, for the estimated decommissioning costs at the end of the producing lives of the group's power stations and wind farms. Capitalised decommissioning costs are depreciated over the useful lives of the related assets. The unwinding of the discount is included within 'Finance costs'.

L. FOREIGN CURRENCIES

Transactions in foreign currencies are translated at the spot rate at the date of the transaction. At the year end, monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date, with exchange gains and losses recognised in the consolidated income statement.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

3 ACCOUNTING POLICIES *continued*

M. TAXATION

The group's and the company's liability for current tax is calculated using the tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on the difference between the carrying amounts of assets and liabilities in the balance sheet and the corresponding tax bases used in the computation of taxable profits (temporary differences), and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which deductible temporary differences, unused tax losses or credits can be utilised.

Deferred tax is calculated on a non-discounted basis at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax is charged in the income statement, except where it relates to items charged or credited to equity (via the statement of comprehensive income), in which case the deferred tax is also dealt with in equity and is shown in the statement of comprehensive income.

N. INVESTMENTS

The company's investments in subsidiaries are stated in the balance sheet at cost, or fair value of shares issued as consideration where applicable. Dividends from subsidiaries are recognised when the right to receive the dividend is established.

4 FINANCIAL RISK MANAGEMENT POLICY

The group's principal financial liabilities, other than derivatives, comprise loans and borrowings and trade and other payables. The main purpose of these financial liabilities is to finance the group's operations. The group has loans and other receivables, trade and other receivables, and cash and short-term deposits that arrive directly from its operations. The group also holds other investments, finance lease receivables and enters into derivative contracts.

During the year ended 31 December 2012, the group has been exposed to energy market risk, credit risk and treasury risk. The group's senior management oversees the management of these risks and details of the governance structure in place is summarised below.

During the year under review the ScottishPower governance structure was supported by risk policies adopted by the ScottishPower Board. These risk policies are adopted and the risk limits and indicators are approved by the ScottishPower Board on an annual basis. ScottishPower business risk assessment teams and the independent group risk management function support the ScottishPower Board in the execution of due diligence and risk management. In addition, the Boards of the group's businesses are responsible for ensuring that their respective businesses' risks are adequately assessed, monitored, mitigated and managed. The UK Risk Director reports on risks for ScottishPower to the ScottishPower Audit and Compliance Committee and such reports are then presented to the ScottishPower Board.

The governance structure ensured that the risk management policies established for each business to identify, assess, monitor, report, manage and mitigate each of the various types of risk involved in its business were adequately designed and implemented and that an effective and efficient system of internal controls was maintained. The businesses adhered to their specific business risk limits and guidelines which were approved by the ScottishPower Board.

The position on risk and strategy for risk management were contained in the Risk Policy for Iberdrola's businesses in the UK (ScottishPower). The ScottishPower Board approved these policies and they were implemented through a rigid risk governance structure, whereby responsibilities were vested with groups, committees and individuals on a global as well as business level. Generally, the risk management policy and control environment ensured that transactions undertaken and instruments used fall into the types of transactions approved by the ScottishPower Board and are properly validated within the appropriate levels of authority. Transactions included instruments such as physically settled instruments, financially-settled instruments, other contractual obligations, regulatory requirements and other obligations. The types of instruments which can be used are approved for each business. Subject to the limit requirements discussed above, no transaction was executed unless it was an approved instrument. Authorised personnel were permitted to engage only in those activities specified in the business operational policies and procedures as approved by the ScottishPower Board.

A clear reporting structure was implemented within the group. It ensured that the portfolios are monitored on a timely basis and sufficient information is made available to management to enable quick response of the business to the dynamic characteristics of its market environment. Those reports included daily position, mark-to-market, Value at Risk ("VaR") reports, as well as periodical fundamentals reports, stress and scenario reports, credit watch, credit exposure, accounting and insurance reports.

Further details of the policies in place to manage exposure to the key risks are detailed in the pages following:

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

4 FINANCIAL RISK MANAGEMENT POLICY *continued*

(a) Energy market risk

The group is exposed to market risk associated with fluctuations in the market price of electricity and generation fuel compounded by volumetric risk caused by unplanned changes in the load and output of its portfolio of generation assets. The risk management policies are implemented at the business level with the oversight of the businesses' Boards, management teams and the independent risk management function. The group uses a number of risk measurement procedures and techniques to ensure that risk is kept within pre-approved limits. The key measures are stop loss limits and volume exposure by tenor limits supported by a daily VaR calculation for controlling earnings volatility and other measures including individual transaction limits. Individual transaction limits are defined by maximum commitment value, physical size, VaR impact, tenor, instrument type and other relevant measures. All valuation models are reviewed and approved by the independent group Risk Management function on an ongoing basis, including changes to assumptions and model inputs. Changes that could have had significant impact on the Accounts required additional review and approval by the appropriate Boards.

VaR is a key measure of the potential financial loss on a price exposure position over a defined period to a given level of confidence. VaR computations for the group's energy commodity portfolios are based on a historical simulation technique or a Monte Carlo simulation technique, which utilises historical or stochastically simulated energy market forward price curve changes to estimate the potential unfavourable impact of price changes in the portfolio positions scheduled to settle within the forward 24 months. The quantification of market risk using VaR provides a consistent measure of risk and sensitivity across the group's continually changing portfolio. VaR is not necessarily indicative of actual results that may occur. Future changes in markets inconsistent with historical data or assumptions used could cause variation in actual results to exceed predicted ranges. The group's VaR computations for its energy commodity portfolio utilise several key assumptions, including a 99% confidence level for the resultant price changes and a holding period of five business days. VaR, while sensitive to changes in portfolio volume, does not account for commodity volume risk. Commodity volume risk is defined as the possibility that a change in the supply of, or demand for, the commodity will create an unexpected imbalance and change the requirements for the commodity. The group applies scenario analysis to reinforce its VaR measurements and uses stochastic analysis to estimate the impact of risk on outcomes.

The group's VaR measures, at 31 December 2012 and over the prior year are shown in the table below.

	2012 £m	2011 £m
VaR	1.8	2.8
Average VaR over prior year	2.4	5.5
Maximum VaR over prior year	6.7	12.6
Minimum VaR over prior year	0.8	1.7

The liberalised business (Energy Wholesale and Energy Retail combined businesses) is exposed to and therefore undertakes activities to manage energy market risk within the group. The hedging activities associated with energy market risk are undertaken within the energy management function. The strategy of the business is to mitigate the economic risks associated with electricity generation, purchase of fuel and supply of electricity and natural gas to end users in both the wholesale and retail markets and also to optimise the value of the asset portfolio. From a reporting perspective the objective is to report earnings results that are consistent with its operational strategies and hence recognise the earnings effect of financial and non-financial derivative transactions executed to hedge economic business risks in the same period in which the hedged operational activity impacts earnings. The aim is to minimise earnings volatility, which would otherwise be present as a result of fair valuing all derivative contracts under IAS 39. To achieve this objective, where effectiveness documentation and reporting requirements are met, cash flow hedge accounting is applied by designation of a series of derivative trades and deferring in equity the fair value changes of open derivative positions until the period in which forecast transactions occur. A number of contracts do not qualify for own use or hedge accounting under IAS 39 and are therefore wholly or partially fair valued through the income statement.

Cash flow hedging strategies are developed for each of the electricity, natural gas, coal and carbon allowances portfolios to hedge the variability in cash flows associated with changes in the market price of each commodity. Forward (fixed price/fixed volume) contracts are designated as hedging instruments in the electricity, gas, and carbon hedges, and financial swaps are designated in the coal hedge.

The electricity, gas, coal and carbon hedges relate to the cash flow variability associated with sales of electricity and purchases of electricity, natural gas, coal and carbon allowances at floating prices that are required to meet forecast demand for each commodity. Forecast demand is based on existing customer numbers and historic profiles of demand at levels that are highly probable of occurring. The associated cash flows extend until 2016 for electricity and gas, and 2015 for coal and carbon allowances.

The assessment of effectiveness of all hedging relationships currently in place is carried out on a monthly basis as part of the financial reporting cycle. Prospective assessment is carried out at inception of the hedge and on an ongoing basis to verify that the forecast is still highly probable of occurring.

Retrospective assessment is also carried out to assess the effectiveness in the period under review. Prospective and retrospective assessment is performed using statistical analysis and the business can apply the hedge accounting rules prescribed by IAS 39 if the hedging relationship passes the criteria of a three-step regression test.

(b) Credit risk

The group is exposed to both settlement risk (defined as the risk of a counterparty failing to pay for energy and/or services which have been delivered), as well as replacement risk (defined as the risk of incurring additional costs in order to replace a sale or purchase contract following a counterparty default). Credit risk is mitigated by contracting with multiple counterparties and limiting exposure to individual counterparties to clearly defined limits based upon the risk of counterparty default.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

4 FINANCIAL RISK MANAGEMENT POLICY *continued*

(b) Credit risk *continued*

Aggregate portfolio risk is monitored and reported by a Credit Value-at-Risk ("CVar") Monte-Carlo-based simulation model to quantify the total credit risk within the existing portfolio.

The group considers that 100% of its credit risk associated with energy-related derivatives can be considered to be with counterparties in related energy industries, financial institutions operating in energy markets or fellow Iberdrola group companies. At the counterparty level the group employs specific eligibility criteria in determining appropriate limits for each prospective counterparty and supplements this with netting and collateral agreements including margining, guarantees, letters of credit and cash deposits where appropriate.

Exposure to credit risk in the supply of electricity and gas arises from the potential customer defaulting on their invoiced payables. The financial strength and credit-worthiness of business customers is assessed prior to commencing, and for the duration of, their contract of supply. Domestic credit worthiness is reviewed from a variety of internal and external information.

At 31 December 2012 and 31 December 2011 the group evaluated the concentration of risk with respect to trade receivables as low, with no material concentration of credit risk in the group arising from one particular counterparty.

The table below shows trade receivables that are past due but not considered impaired. These relate primarily to retail customers who have not paid the outstanding balance within agreed payment terms:

	2012 £m	2011 £m
Past due but not impaired:		
Less than 3 months	96.7	78.9
Between 3 and 6 months	15.8	16.2
Between 6 and 12 months	11.9	17.3
After more than 12 months	3.8	7.7
	128.2	120.1

The requirement for an impairment is analysed at each reporting date and this is estimated by management taking into account future cash flows, prior experience, ageing analysis and an assessment of the current economic climate within which the group operates.

The maximum exposure to credit risk in respect of trade receivables is the carrying value of the trade receivables at the balance sheet date. The carrying value of trade receivables is stated net of the allowance for impairment.

(c) Treasury risk

Treasury risk is comprised of liquidity risk and market risk. The group's cash management and short-term financing activity is integrated with ScottishPower whose activities are themselves integrated with its ultimate parent company, Iberdrola S.A.. ScottishPower's financing structure is determined largely by its position in the wider Iberdrola group. As a result, ScottishPower's credit rating is related to that of Iberdrola S.A.. As at 31 December 2012 ScottishPower's long-term credit ratings were Baa1 and BBB from Moody's and Standard & Poor's respectively.

(i) Treasury liquidity risk

Liquidity risk, the risk that the group will have insufficient funds to meet its liabilities, is managed by Iberdrola group treasury, who are responsible for arranging banking facilities on behalf of ScottishPower and so the group. For the purposes of the group, Scottish Power Limited is the principal counterparty for the loan balances due to and from the subsidiaries of the Scottish Power UK plc.

The table below summarises the maturity profile of the group's financial liabilities as at 31 December 2012 and 31 December 2011 based on contractual undiscounted payments.

Financial liabilities (excluding commodity derivatives)

	2012						Total £m
	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 and thereafter £m	
Cash outflows							
Derivative financial instruments (excluding commodity derivatives)	1,094.5	292.2	100.3	39.9	–	–	1,526.9
Loans and other borrowings	3,497.4	137.0	138.0	138.8	339.6	3,035.8	7,286.6
Payables*	1,232.3	2.1	2.0	2.0	–	–	1,238.4
	5,824.2	431.3	240.3	180.7	339.6	3,035.8	10,051.9
	2011						Total £m
	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 and thereafter £m	
Cash outflows							
Derivative financial instruments (excluding commodity derivatives)	633.0	120.2	12.9	12.1	9.7	–	787.9
Loans and other borrowings	2,190.8	100.8	100.9	101.6	102.6	2,755.1	5,351.8
Payables*	1,283.6	0.7	1.1	2.0	–	–	1,287.4
	4,107.4	221.7	114.9	115.7	112.3	2,755.1	7,427.1

* Contractual cash flows exclude accrued interest as these cash flows are included within loans and other borrowing

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

4 FINANCIAL RISK MANAGEMENT POLICY *continued*

(c) Treasury risk *continued*

(i) Treasury liquidity risk *continued*

Commodity derivatives

The group believes the liquidity risk associated with commodity derivatives needs to be considered in conjunction with the profile of payments in relation to all derivative contracts rather than only those in a liability position. It should be noted that cash flows associated with future energy sales and commodity contracts which are not IAS 39 financial instruments are not included in this analysis, which is prepared in accordance with IFRS 7 'Financial Instruments: Disclosures' ('IFRS 7').

	2012						
	Less than 1 year £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	Over 5 years £m	Total £m
Net cash outflows	855.6	590.9	379.2	250.2	86.4	–	2,162.3

	2011						
	Less than 1 year £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	Over 5 years £m	Total £m
Net cash outflows	875.9	702.9	518.9	442.6	368.9	91.4	3,000.6

Details of the group's contractual commitments are given in Note 31.

(ii) Treasury market risk

Market risk is the risk of loss that results from changes in market rates (foreign exchange rates and interest rates). Within the Treasury function the group utilises a number of financial instruments to manage interest rate and foreign currency exposures.

The table below shows the debt structure of the group, after taking hedging derivatives into account.

Interest rate analysis of debt

	2012 £m	2011 £m
Variable rate	3,993.1	2,546.2
Fixed rate	1,733.5	1,387.0
	5,726.6	3,933.2

The reference interest rates for the floating rate borrowings are London Inter Bank Offer Rate ("LIBOR"), Euro Bank Offered Rate ("EURIBOR"), Bank of England Base Rate ("Base") and includes borrowings linked to the Retail Price Index ("RPI").

The variable rate debt consists of £83.4 million Japanese Yen ("JPY") loan, £252.0 million inflation linked bonds, £189.1 million LIBOR linked debt, £107.1 million EURIBOR linked debt and £3,361.5 million repayable on demand which is linked to Base.

The interest on JPY debt is fixed, however this is changed to variable by a cross currency swap. Interest is based on the Sterling LIBOR curve. For indicative purposes, a 1% increase in LIBOR would result in a £0.5 million increase in the full year interest charge.

For the inflation linked bonds, a 10% increase in the rate of change of RPI would result in a £0.1 million increase in the full year interest charge.

For LIBOR and EURIBOR linked debt, a 1% increase in the rate would result in a £2.9 million increase in the full year interest charge.

The interest rate on the short-term variable rate debt is linked to Base, which is not expected to change in the short term.

Cash flow hedges

Hedging of commodity purchases: Where commodities are priced in a currency other than Sterling, the foreign exchange risk is hedged using forward foreign exchange contracts. These are designated as cash flow hedges where they comply with the requirements of IAS 39.

Hedging of asset purchases: The group is subject to cash flow risk resulting from the purchase of various assets which are denominated in foreign currencies. The risk being hedged relates to the fluctuation in the functional currency terms of value of these foreign denominated purchases. The group enters into forward foreign exchange rate contracts to hedge those risks.

Hedging the value of currency denominated intercompany loans: The group has provided funding to or received funding from other Iberdrola companies denominated in currencies other than Sterling. The value of the group's asset or liabilities in relation to this funding is subject to foreign exchange risk. As a result, the group enters into cross currency swaps or foreign exchange rate contracts as hedges and has designated those within a cash flow hedging relationship where they meet the required hedging criteria.

Fair value hedges

Hedging the value of issued sterling debt: During the prior year, the group had a medium-term loan at a fixed interest rate, which was designated in a hedging relationship, hedged by a variable to fixed interest rate swap. The objective of this hedging strategy was to protect the value of the group's fixed loan note from changes as a result of fluctuations of the market interest rates.

Hedging the value of cross currency debt: The group has issued debt instruments denominated in JPY. The value of the group's liability with respect to those instruments is subject to foreign exchange risk and interest rate risk. As a result the group has entered into cross-currency swaps as hedges and has designated those within a fair value hedging relationship where they meet required hedging criteria.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

4 FINANCIAL RISK MANAGEMENT POLICY *continued*

(c) Treasury risk *continued*

(ii) Treasury market risk *continued*

Hedge assessment

Hedge assessment is done prospectively to verify that the forecast transactions are still highly probable of occurring (for cash flow hedges) as well as retrospectively, to assess the effectiveness in the period under review. Prospective assessment is performed using sensitivity analysis and critical terms matching. Retrospective assessment is performed using the dollar offset approach which compares the change in fair value of the hedging instrument with the hedged item, to determine whether a high level of correlation exists between those changes.

5 CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In determining and applying accounting policies, judgement is often required in respect of items where the choice of specific policy to be followed could materially affect the reported amounts of revenues, expenses, assets and liabilities of the group should it later be determined that a different choice would be more appropriate. Such a policy is discussed at (a) below. In addition, in preparing the consolidated Accounts in conformity with IFRS, the company is required to make estimates and assumptions that impact on the reported amounts of revenues, expenses, assets and liabilities of the group. Actual results may differ from these estimates. These are discussed at (b) to (j) below. These critical accounting judgements and key sources of estimation uncertainty should be read in conjunction with the full statement of Accounting Policies at Note 3.

(a) EMISSIONS ALLOWANCES

In accordance with the group accounting policy, purchased emissions allowances are initially recognised at cost within intangible assets. Allocated allowances awarded to the group by the government or a similar body are recorded initially at their fair value with a corresponding credit to deferred income which is released to the income statement in line with the expected emissions over the period covered by the allowances. The group recognises liabilities in respect of its obligations to deliver emissions allowances. Any liabilities recognised are measured based on the value at which these allowances were initially recognised on the balance sheet. If it is estimated that it will be necessary to deliver more emission allowance than recorded on the balance sheet the liability to this shortfall is calculated based on the market price of the allowances at the balance sheet date.

(b) FINANCIAL INSTRUMENTS

IAS 39 requires certain financial instruments, in particular derivatives, to be recorded as assets and liabilities in the balance sheet. The group's valuation strategy for these financial instruments is to utilise, as far as possible, quoted prices in an active trading market. In the absence of quoted prices for identical or similar assets or liabilities, it is sometimes necessary to apply valuation techniques where contracts are marked to approved models. Models are used for developing both the forward curves and the valuation metrics of the instruments themselves where the instruments are complex combinations of standard or non-standard products. All models are subject to rigorous testing prior to being approved for valuation and subsequent continuous testing and approval procedures designed to ensure the validity and accuracy of the model assumptions and inputs.

The assumptions within the models used to value financial instruments are critical, since any changes in assumptions could have a significant impact on the fair values and movements which are reflected in the group income statement, group statement of comprehensive income and group balance sheet. There is little formal guidance to assist in applying IAS 39 to the group's energy management activities. As a result, significant judgements must be made in applying IAS 39 to the group's energy contracts in particular. Disclosures relating to the group's VaR measures and derivative financial instruments are set out in Notes 4 and 19 respectively.

At 31 December 2012, the carrying value of derivative financial assets was £336.6 million (2011 £551.9 million) and the carrying value of derivative financial liabilities was £357.8 million (2011 £513.8 million).

(c) REVENUE

The nature of the energy industry in the UK in which the group operates is such that the group's revenue recognition is subject to a degree of estimation. The assessment of energy sales to retail customers is based on meter readings, which are carried out on a systematic basis throughout the year. Revenue from the sale of energy to retail customers is the value of units supplied during the year and includes an estimate of the value of the units supplied to customers between the date of their last meter reading and the period end based on external data supplied by the electricity and gas market settlement process. At the end of each accounting period, amounts of energy delivered to customers since the last billing date are estimated and the corresponding unbilled revenue is estimated and recorded in revenue.

Billed revenue not yet received is included in trade receivables and unbilled revenue is included within accrued income in the consolidated balance sheet. Billed and unbilled revenue relating to the group's retail customers included within the consolidated balance sheet at 31 December 2012 amounted to £283.5 million (2011 £322.9 million).

(d) IMPAIRMENT OF TRADE RECEIVABLES

Trade receivables are stated net of allowance for impairment of doubtful debts. The group estimates its provision for impairment taking into account future cash flows, based on prior experience, ageing analysis and an assessment of the current economic environment within which the group operates. Such estimates involve a significant degree of judgement.

The provision for impairment of trade receivables at 31 December 2012 amounted to £44.5 million (2011 £54.5 million) and trade receivables and accrued income (net of the provision for impairment) amounted to £714.1 million (2011 £839.8 million).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

5 CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY *continued*

(e) IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

In certain circumstances, property, plant and equipment are required to be reviewed for impairment. When a review for impairment is conducted, the recoverable amount is assessed by reference to the net present value of the expected future cash flows of the relevant Cash Generating Unit ("CGU"), or disposal value if higher. The discount rate applied is based on the group's weighted average cost of capital with appropriate adjustments for the risks associated with the CGU. Estimates of cash flows involve a significant degree of judgement and are consistent with management's plans and forecasts.

At 31 December 2012, the carrying value of property, plant and equipment amounted to £8,999.1 million (2011 £6,454.3 million).

(f) CONTINGENCIES

Appropriate recognition and disclosure of contingent liabilities is made regarding litigation, tax matters, and environmental issues, among others. Accounting for contingencies requires significant judgement by management regarding the estimated probabilities and ranges of exposure to potential loss. The evaluation of these contingencies is performed by various specialists inside and outside of the group.

The company's assessment of the group's exposure to contingencies could change as new developments occur or more information becomes available. The outcome of the contingencies could vary significantly and could materially impact the group's results and financial position. The company has used its best judgement in applying IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' to these matters.

(g) RETIREMENT BENEFITS

The group operates a number of defined benefit schemes for its employees which are accounted for in accordance with IAS 19 'Employee Benefits' using the immediate recognition approach.

The expense and balance sheet items relating to the group's accounting for pension schemes under IAS 19 are based on actuarial valuations. Inherent in these valuations are key assumptions, including discount rates, earnings increases, mortality and increases in pensions in payment. These actuarial assumptions are reviewed annually in line with the requirements of IAS 19. The assumptions adopted are based on prior experience, market conditions and the advice of plan actuaries.

At 31 December 2012, the liability in the balance sheet for retirement benefit obligations amounted to £498.7 million (2011 £212.1 million), respectively. Sensitivity disclosures relating to the group's retirement benefit obligations are set out in Note 16.

(h) DECOMMISSIONING AND ENVIRONMENTAL

The group periodically revises the estimates made concerning the costs to be incurred in the decommissioning of the group's power plants (including wind farms) and the obligation to remove asbestos from the power stations over the course of their operational lives. At 31 December 2012, the present value of the aforementioned costs amounted to £111.8 million (2011 £73.9 million).

(i) REGULATORY PROVISIONS

The group has recognised a provision for Regulatory costs. In determining the fair value of the provision, assumptions and estimates are made in relation to the expected value and timing of these costs. The carrying amount of the provision as at 31 December 2012 was £29.7 million (2011 £21.5 million).

(j) ROC RECYCLE INCOME

As a renewable energy generator, the group's Renewables business receives ROC recycle income. Income is accrued monthly based on Renewables output volumes and an estimated price per unit. The estimated price is calculated factoring in the total UK renewable energy output, generation capacity and demand. The actual price is announced by Ofgem in October each year for the year ended 31 March, following which the estimated income number is adjusted accordingly.

The ROC recycle income for the year ended 31 December 2012 was £4.0 million (2011 £nil).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

6 BUSINESS SEGMENT REPORTING

(a) Operating segments and business divisions

The classification of the group's operating segments for management reporting purposes are based on a combination of factors, principally differences in products and services and the regulatory environment within which each business operates.

For management reporting purposes the group is currently organised into four operating segments, Energy Networks, Energy Wholesale, Energy Retail and Renewables, as detailed in Note 1 of the Accounts. In order to comply with the requirements of IFRS 8 'Operating Segments', the group therefore reports its operating segments on this basis and the measure of profit used for the purpose of reporting to the Chief Operating Decision Maker ("CODM") is profit from operations as per the consolidated income statement. All revenue and profit from operations arise from operations within Great Britain and Ireland.

In order to provide the key stakeholders of the Accounts with further relevant and transparent information, the group has voluntarily disclosed revenue and profit from operations for the Generation, Supply and Energy Management divisions within the Energy Wholesale, Energy Retail and Renewables operating segments, whilst also providing detail in relation to non-recurring items and certain measurements arising from IAS 39, consistent with the Supply and Generation regulatory licence conditions. This information has been calculated, where appropriate, in accordance with Standard Licence Condition 16B of the Electricity Generation Licence and Standard Condition 19A of the Electricity and Gas Supply Licences.

The group's operating segments and business divisions are as follows:

Operating Segment	Business Divisions	Business Division Description
Energy Networks	<i>Energy Networks</i>	The transmission and distribution business within the ScottishPower group.
Energy Wholesale	<i>Generation – Licensed business¹</i>	The licensed activity of the Energy Wholesale operating segment.
	<i>Energy Management¹</i>	The non-licensed activities of the Energy Wholesale operating segment, responsible for wholesale market sales and purchases for the Generation and Supply licensed business divisions.
	<i>Other</i>	The other non-licensed activity of the Energy Wholesale operating segment division which includes the results of the group's waste water treatment facility.
Energy Retail	<i>Supply – Licensed business¹</i>	The licensed activity of the Energy Retail operating segment.
	<i>Other</i>	The non-licensed activity of the Energy Retail operating segment which includes the group's energy services activity.
Renewables	<i>Generation – Licensed business¹</i>	The Great Britain licensed activity of the group's Renewables operating segment.
	<i>Other</i>	The non-licensed activity of the Renewables operating segment, which includes generation activity outwith Great Britain and the impact of the amortisation of the fair value attributed to the Renewables segment when purchased by Iberdrola during 2007. Refer to Note 34 for further information.

¹ The Generation – Licensed, Supply – Licensed and the Energy Management businesses are consistent with those disclosed in the Consolidated Segmental Statements for the Supply and Generation licensed businesses presented in accordance with Standard Licence Condition 16B of the Electricity Generation Licence and Standard Condition 19A of the Electricity and Gas Supply Licences. These statements can be found at www.scottishpower.com/pages/company_reporting.asp

During the year the group also reviewed the classification of business support costs for segmental purposes (previously shown separately within the unallocated business). These are now allocated across each of the operating segments and business divisions in the segmental analysis below.

Comparative numbers have been restated accordingly.

(b) Revenue by operating segment and business division

(i) Revenue by operating segment

Revenue by operating segment for the year ended 31 December 2012

Operating Segment	External Revenue £m	Inter-segment Revenue £m	Total Revenue £m
Energy Networks	738.6	230.6*	969.2
Energy Wholesale	3,252.6	2,274.2	5,526.8
Energy Retail	3,799.4	18.8	3,818.2
Renewables	12.5	201.2	213.7
Elimination of inter-segment revenue			(2,724.8)
			7,803.1

* Inter-segment revenue relating to Energy Networks is predominantly subject to regulation and is based on published tariffs set by the regulator.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

6 BUSINESS SEGMENT REPORTING *continued*

(b) Revenue by operating segment and business division *continued*

(i) Revenue by operating segment *continued*

Revenue by operating segment for the year ended 31 December 2011

Operating Segment	External Revenue £m	Inter-segment Revenue £m	Total Revenue £m
Energy Networks	677.6	227.8*	905.4
Energy Wholesale	2,412.6	2,259.1	4,671.7
Energy Retail	3,350.7	20.0	3,370.7
Renewables	–	–	–
Elimination of inter-segment revenue			(2,506.9)
			6,440.9

* Inter-segment revenue relating to Energy Networks is predominantly subject to regulation and is based on published tariffs set by the regulator.

(ii) Additional Information – Revenue by business division

Revenue by business division for the year ended 31 December 2012

Operating Segment	Business Division	External Revenue £m	Inter-segment Revenue £m	Total Revenue £m
Energy Networks		738.6	230.6	969.2
	Generation – Licensed business	104.6	1,079.2	1,183.8
	Energy Management	3,148.0	2,771.1	5,919.1
	<i>Elimination of internal segmental revenue</i>	–	(1,576.1)	(1,576.1)
Energy Wholesale		3,252.6	2,274.2	5,526.8
	Supply – Licensed business	3,796.8	18.8	3,815.6
	Other	2.6	–	2.6
Energy Retail		3,799.4	18.8	3,818.2
	Generation – Licensed business	0.6	196.7	197.3
	Other	11.9	4.5	16.4
Renewables		12.5	201.2	213.7
Elimination of inter-segment revenue				(2,724.8)
Total				7,803.1

Revenue by business division for the year ended 31 December 2011

Operating Segment	Business Division	External Revenue £m	Inter-segment Revenue £m	Total Revenue £m
Energy Networks		677.6	227.8	905.4
	Generation – Licensed business	790.1	933.9	1,724.0
	Energy Management	1,622.5	1,396.7	3,019.2
	<i>Elimination of internal segmental revenue</i>	–	(71.5)	(71.5)
Energy Wholesale		2,412.6	2,259.1	4,671.7
	Supply – Licensed business	3,350.2	20.0	3,370.2
	Other	0.5	–	0.5
Energy Retail		3,350.7	20.0	3,370.7
	Generation – Licensed business	–	–	–
	Other	–	–	–
Renewables		–	–	–
Elimination of inter-segment revenue				(2,506.9)
Total				6,440.9

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

6 BUSINESS SEGMENT REPORTING *continued*

(c) Profit from operations by operating segment and business division

(i) Profit from operations by operating segment

Profit from operations by operating segment for the year ended December 2012

	Profit/(loss) from operations reported to the CODM £m
Operating Segment	
Energy Networks	601.9
Energy Wholesale	(1.6)
Energy Retail	169.5
Renewables	63.8
Unallocated	19.5
Total	853.1

Profit from operations by operating segment for the year ended December 2011

	Profit/(loss) from operations reported to the CODM £m
Operating Segment	
Energy Networks	551.2
Energy Wholesale	(161.0)
Energy Retail	(21.8)
Renewables	–
Unallocated	1.1
Total	369.5

(ii) Additional information – Profit from operations by business division

Profit from operations by business division for the year ended 31 December 2012

Operating Segment	Business Division	Profit/ (loss) from operations reported to the CODM £m	Non-recurring items (Note (iii)) £m	Certain remeasurements (Note (iv)) £m	Adjusted profit/ (loss) from operations as per regulatory licence requirements* £m
Energy Networks		601.9	–	–	601.9
	Generation – Licensed business	(51.6)	3.9	50.7	3.0
	Energy Management	48.0	0.8	(46.0)	2.8
	Other	2.0	0.5	–	2.5
Energy Wholesale		(1.6)	5.2	4.7	8.3
	Supply – Licensed business	165.8	9.7	–	175.5
	Other	3.7	1.3	–	5.0
Energy Retail		169.5	11.0	–	180.5
	Generation – Licensed business	90.4	1.0	–	91.4
	Other	(26.6)	–	–	(26.6)
Renewables		63.8	1.0	–	64.8
Unallocated		19.5	(17.0)	–	2.5
Total		853.1	0.2	4.7	858.0

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

6 BUSINESS SEGMENT REPORTING *continued*

(c) Profit from operations by operating segment and business division *continued*

(ii) Additional information – Profit from operations by business division *continued*

Profit from operations by business division for the year ended 31 December 2011

Operating Segment	Business Division	Profit from operations reported to the CODM £m	Non-recurring items (Note (iii)) £m	Certain remeasurements (Note (iv)) £m	Adjusted profit from operations as per regulatory licence requirements* £m
Energy Networks		551.2	(1.1)	–	550.1
	Generation – Licensed business	(30.4)	161.6	39.9	171.1
	Energy Management	(138.1)	2.6	21.9	(113.6)
	Other	7.5	–	–	7.5
Energy Wholesale		(161.0)	164.2	61.8	65.0
	Supply – Licensed business	(21.5)	27.3	–	5.8
	Other	(0.3)	0.7	–	0.4
Energy Retail		(21.8)	28.0	–	6.2
	Generation – Licensed business	–	–	–	–
	Other	–	–	–	–
Renewables		–	–	–	–
Unallocated		1.1	1.3	–	2.4
Total		369.5	192.4	61.8	623.7

*Standard Licence Condition 16B of the Electricity Generation Licence and Standard Condition 19A of the Electricity and Gas Supply Licences.

(iii) Non-recurring items

In the year ended 31 December 2012 the following non-recurring items were recorded:

Provisions for restructuring and other liabilities: On review of the group's provisions as at 31 December 2012, restructuring provisions and associated pension costs of £13.6 million were recognised. In addition, the group recognised £8.9 million for future costs associated with various regulatory reviews and contractual obligations.

Impairment and non-current asset write-offs: During the year ended 31 December 2012, following the cancellation of certain capitalised development projects, £4.0 million of impairment charges were recognised in the year and £3.0 million of assets no longer in use were written-off to the income statement.

Operating Income: During the year ended 31 December 2012, non-recurring operating income of £13.5 million was recognised on settlement of outstanding insurance claims and following a review of the business combinations transactions which took place during 2011 non-recurring income of £15.8 million was recognised.

In the year ended 31 December 2011 the following non-recurring items were recorded:

Provisions for restructuring and other liabilities: On review of the group's provisions as at 31 December 2011, restructuring provisions and associated pension costs of £12.4 million were recognised. In addition, the group recognised £21.5 million for future costs associated with various regulatory reviews and contractual obligations.

Impairment of generation assets arising from changing market conditions: During the year ended 31 December 2011 a net impairment charge of £158.5 million comprised a charge of £150.8 million resulting from a reassessment of the operational life of the Longannet coal-fired fuel plant and a net charge of £7.7 million resulting from the cancellation of capitalised development projects and associated capital grants, principally in respect of Carbon Capture.

(iv) Certain remeasurements

Certain remeasurements arising from IAS 39 have been disclosed separately to aid the understanding of the underlying performance of the group.

(d) Other financial data by operating segment

	Acquisition of property, plant and equipment and intangible assets reported to the CODM £m	Depreciation, amortisation and impairment reported to the CODM £m	Impairment of trade receivables reported to the CODM £m
Other items by segment for the year ended 31 December 2012			
Energy Retail	629.0	172.2	0.2
Energy Wholesale	155.2	135.9	0.1
Energy Retail	142.7	3.3	32.0
Renewables	317.1	76.4	–
Unallocated	14.3	23.1	5.8
Total	1,258.3	410.9	38.1
Other items by segment for the year ended 31 December 2011			
Energy Retail	517.2	155.0	5.0
Energy Wholesale	232.0	286.8	–
Energy Retail	3.5	1.8	49.8
Renewables	–	–	–
Unallocated	7.2	35.5	0.1
Total	759.9	479.1	54.9

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

7 INTANGIBLE ASSETS

(a) Movements in intangible assets

Year ended 31 December 2011	Note	Goodwill £m	Other intangible assets				Total £m	Total £m
			Computer software (Note (ii)) £m	Emissions allowances (Note (iii)) £m	Licences £m	Other (Note (iii)) £m		
Cost:								
At 1 January 2011		90.1	449.7	184.3	9.5	–	643.5	733.6
Business combinations	(v)	–	14.3	13.3	–	–	27.6	27.6
Additions		–	12.4	133.9	–	–	146.3	146.3
Disposals		–	(9.1)	–	–	–	(9.1)	(9.1)
Delivery of emissions allowances		–	–	(185.4)	–	–	(185.4)	(185.4)
At 31 December 2011		90.1	467.3	146.1	9.5	–	622.9	713.0
Amortisation:								
At 1 January 2011		8.0	358.4	–	1.1	–	359.5	367.5
Business combinations	(v)	–	9.1	–	–	–	9.1	9.1
Amortisation for the year		–	35.3	–	0.3	–	35.6	35.6
Disposals		–	(6.6)	–	–	–	(6.6)	(6.6)
At 31 December 2011		8.0	396.2	–	1.4	–	397.6	405.6
Net book value:								
At 31 December 2011		82.1	71.1	146.1	8.1	–	225.3	307.4
At 1 January 2011		82.1	91.3	184.3	8.4	–	284.0	366.1

Year ended 31 December 2012	Notes	Goodwill £m	Other intangible assets				Total £m	Total £m
			Computer software (Note (ii)) £m	Emissions allowances (Note (iii)) £m	Licences £m	Other (Note (iii)) £m		
Cost:								
At 1 January 2012		90.1	467.3	146.1	9.5	–	622.9	713.0
Business combinations	(iv)	364.6	1.6	–	–	532.4	534.0	898.6
Transfer from an Iberdrola group company	(vi)	–	138.5	–	–	–	138.5	138.5
Additions		–	17.2	63.1	–	–	80.3	80.3
Transfer to property, plant and equipment		–	–	–	–	(42.0)	(42.0)	(42.0)
Disposals		–	–	–	–	(4.0)	(4.0)	(4.0)
Delivery of emissions allowances		–	–	(144.3)	–	–	(144.3)	(144.3)
At 31 December 2012		454.7	624.6	64.9	9.5	486.4	1,185.4	1,640.1
Amortisation:								
At 1 January 2012		8.0	396.2	–	1.4	–	397.6	405.6
Business combinations	(iv)	–	0.4	–	–	4.8	5.2	5.2
Amortisation for the year		–	36.5	–	0.4	0.8	37.7	37.7
Disposals		–	–	–	–	(1.9)	(1.9)	(1.9)
At 31 December 2012		8.0	433.1	–	1.8	3.7	438.6	446.6
Net book value:								
At 31 December 2012		446.7	191.5	64.9	7.7	482.7	746.8	1,193.5
At 1 January 2012		82.1	71.1	146.1	8.1	–	225.3	307.4

- (i) The cost of fully amortised computer software still in use at 31 December 2012 was £350.1 million (2011 £298.2 million).
- (ii) The carrying value of allocated emissions allowances at 31 December 2012 was £56.1 million (2011 £125.4 million). In line with the use of the cost model for subsequent measurement of such allowances, these carrying values equate to the fair values of these allowances at the dates of their allocation.
- (iii) The 'Other' category of intangible assets comprises licence amounts relating to the acquisition of land rights and the value attributed to future renewables projects recognised by Iberdrola S.A. on acquisition of SPREL.
- (iv) On 1 January 2012, as part of an Iberdrola group restructuring exercise, the group acquired certain renewable energy companies from another Iberdrola group company, as set out in Note 34. The cost of goodwill recognised as part of this business combination under common control amounted to £364.6 million. The cost of other intangible assets recognised, amounted to £534.0 million and the related aggregate amortisation amounted to £5.2 million.
- (v) On 1 July 2011 as part of a group restructuring exercise, the group acquired certain subsidiaries from SPUKH as set out in Note 34. The cost of intangible assets recognised as part of this business combination under common control, amounted to £27.6 million and the related aggregate amortisation recognised amounted to £9.1 million.
- (vi) On 31 December 2012, the ultimate parent company, Iberdrola S.A. transferred computer software costs of £138.5 million (2011 £nil) relating to the development and implementation of new customer billing systems to a group company. This remains in the development stage and amortisation will not be charged until the assets become fully operational.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

7 INTANGIBLE ASSETS *continued*

(b) Impairment tests for goodwill

The group holds goodwill in respect of Rye House power station (see (i) below) and its Renewables business (see (ii) below). The recoverable amounts for both have been determined based on value-in-use calculations. These calculations use cash flow projections which reflect past experience and which are based upon a management approved business plan, ending in 2020. Cash flows beyond that period reflect asset estimated useful lives as well as management's forward view of commodity prices and the business strategic objectives. It is considered appropriate to assess the cash flows over a period longer than five years as this better reflects the long term nature of energy market operations and governance and of wind farm development lead times.

(i) Rye House

The carrying amount of goodwill for Rye House power station at 31 December 2012 was £82.1 million (2011 £82.1 million).

The value-in-use calculation is based on generation output over the expected life of the station. Forecasts of station availability and efficiency are based on management expectations and past experience. Price forecasts include wholesale power prices and input costs such as wholesale gas prices and carbon emission costs. The value-in-use calculation also takes into account the extrinsic value of the power station as calculated by a widely recognised option pricing model. The extrinsic value of the station represents the additional value of the station from the capture of short-term volatilities in commodity prices.

Other cash outflows are based on planned operating and capital expenditure.

The impairment test showed a recoverable amount which exceeded the carrying amount. Reasonably possible changes in key assumptions could cause Rye House's recoverable amount to be lower than the carrying value. A reduction in commodity related contribution greater than £5.8 million or an increase in discount rate of greater than 20 basis points would result in the recoverable amount being lower than the carrying amount.

Main assumptions used for value-in-use calculations

Growth rate (beyond the period covered by the business plan)
2.5% nominal, 0% real
Discount rate (pre-tax) 7.22% (used to calculate extrinsic value)
Forward price of underlying commodities
Volatility of underlying commodities (used to calculate extrinsic value)
Correlations of underlying commodities (used to calculate extrinsic value)

Basis for determining values assigned to key assumptions

Use of a 0% real growth rate is derived from past experience and future expectations for the station
Discount rate is determined on the basis of market data and the divisional cost of capital
Market quotes/management future expectations
Market quotes/historical analysis
Historical analysis

(ii) Renewables

The carrying amount of goodwill for the Renewables business at 31 December 2012 was £364.6 million (2011 £nil).

The value-in-use calculation is based on anticipated generation output over the expected lives of individual wind farm projects.

Cash inflows for all projects are based on anticipated generation output based on wind studies and past experience and are valued at forward power prices based on observable market information where available, assumed continuing government support through ROCs and other mechanisms and on internal model assumptions.

Cash outflows are based on planned operating and capital expenditure.

The value-in-use calculation of the Renewables business exceeds the carrying value. Management believes that any reasonably possible change in the key assumptions on which the value-in-use calculation is based would not cause a change to this conclusion. The expected forward price of power and discount rates applied are the key assumptions to which the value-in-use calculation is most sensitive. The value-in-use still exceeds the carrying value with any reasonably possible reduction of the forward price of power or increase of discount rate.

Main assumptions used for value-in-use calculations

Discount rate (pre-tax) Onshore 6.77%, Offshore 7.89%
Forward price of power

Basis for determining values assigned to key assumptions

Discount rate is determined on the basis of market data and the divisional cost of capital
Market quotes/management future expectations

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

8 PROPERTY, PLANT AND EQUIPMENT

(a) Movements in property, plant and equipment

	Notes	Total operating plant (see Note (b)) £m	Other items of property, plant and equipment in use £m	Plant in progress £m	Other items of property, plant and equipment in progress £m	Total £m
Year ended 31 December 2011						
Cost:						
At 1 January 2011		7,250.2	341.7	1,109.5	20.1	8,721.5
Business combinations	(vi)	349.6	22.7	12.8	2.3	387.4
Additions		12.1	6.7	581.3	13.5	613.6
Transfers from in progress to in plant use		556.3	4.9	(561.2)	–	–
Transfer to fellow Iberdrola group company	(v)	–	(5.7)	(3.7)	–	(9.4)
Disposals		(48.7)	(3.8)	–	(14.9)	(67.4)
Impairment	(iv)	–	–	(93.6)	–	(93.6)
At 31 December 2011		8,119.5	366.5	1,045.1	21.0	9,552.1
Depreciation:						
At 1 January 2011		2,518.9	177.4	–	–	2,696.3
Business combinations	(vi)	99.3	0.5	–	–	99.8
Charge for the year		261.3	13.1	–	–	274.4
Disposals		(44.8)	(3.4)	–	–	(48.2)
Impairment	(iv)	75.5	–	–	–	75.5
At 31 December 2011		2,910.2	187.6	–	–	3,097.8

Net book value:

At 31 December 2011	5,209.3	178.9	1,045.1	21.0	6,454.3
At 1 January 2011	4,731.3	164.3	1,109.5	20.1	6,025.2

The net book value of property, plant and equipment at 31 December 2011 is analysed as follows:

Property, plant and equipment in use	5,209.3	178.9	–	–	5,388.2
Property, plant and equipment in the course of construction	–	–	1,045.1	21.0	1,066.1
	5,209.3	178.9	1,045.1	21.0	6,454.3

	Notes	Total operating plant (see Note (b)) £m	Other items of property, plant and equipment in use £m	Plant in progress £m	Other items of property, plant and equipment in progress £m	Total £m
Year ended 31 December 2012						
Cost:						
At 1 January 2012		8,119.5	366.5	1,045.1	21.0	9,552.1
Business combinations	(vi)	1,740.6	5.7	459.8	–	2,206.1
Additions		52.8	13.7	966.7	6.3	1,039.5
Transfers from in progress to plant in use		1,410.4	4.7	(1,412.9)	(2.2)	–
Transfers from intangible assets		–	–	42.0	–	42.0
Transfer from inventories	(vii)	–	–	–	11.7	11.7
Disposals		(124.3)	(7.3)	(1.1)	(3.7)	(136.4)
Impairment	(iv)	–	–	(1.0)	(3.0)	(4.0)
At 31 December 2012		11,199.0	383.3	1,098.6	30.1	12,711.0
Depreciation:						
At 1 January 2012		2,910.2	187.6	–	–	3,097.8
Business combinations	(vi)	368.7	0.5	–	–	369.2
Charge for the year		358.7	10.5	–	–	369.2
Disposals		(118.7)	(5.6)	–	–	(124.3)
At 31 December 2012		3,518.9	193.0	–	–	3,711.9

Net book value:

At 31 December 2012	7,680.1	190.3	1,098.6	30.1	8,999.1
At 1 January 2012	5,209.3	178.9	1,045.1	21.0	6,454.3

The net book value of property, plant and equipment at 31 December 2012 is analysed as follows:

Property, plant and equipment in use	7,680.1	190.3	–	–	7,870.4
Property, plant and equipment in the course of construction	–	–	1,098.6	30.1	1,128.7
	7,680.1	190.3	1,098.6	30.1	8,999.1

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

8 PROPERTY, PLANT AND EQUIPMENT *continued*

(b) The movements in total operating plant are analysed as follows:

Year ended 31 December 2011	Hydro-electric plants £m	Fossil fuel plants £m	Combined cycle plants £m	Wind power plants £m	Gas storage facilities £m	Transmission facilities £m	Distribution facilities £m	Meters and measuring devices £m	Other facilities (see Note (viii)) £m	Total operating plant £m
Cost:										
At 1 January 2011	128.9	1,040.3	555.5	–	10.6	1,016.9	3,983.6	347.9	166.5	7,250.2
Business combinations	–	–	325.8	–	23.8	–	–	–	–	349.6
Additions	–	–	–	–	–	–	–	12.1	–	12.1
Transfers from in progress to plant in use	9.8	49.1	34.3	–	0.5	167.5	288.8	(3.4)	9.7	556.3
Disposals	(0.2)	(17.0)	(3.4)	–	–	(7.3)	(16.7)	(2.5)	(1.6)	(48.7)
At 31 December 2011	138.5	1,072.4	912.2	–	34.9	1,177.1	4,255.7	354.1	174.6	8,119.5

Depreciation:

At 1 January 2011	60.1	688.6	203.4	–	0.6	294.8	996.1	194.4	80.9	2,518.9
Business combinations	–	–	90.6	–	8.7	–	–	–	–	99.3
Charge for the year	5.0	65.2	40.8	–	0.6	20.5	93.3	26.3	9.6	261.3
Disposals	–	(17.0)	(3.4)	–	–	(6.1)	(15.7)	(1.9)	(0.7)	(44.8)
Impairment	–	75.5	–	–	–	–	–	–	–	75.5
At 31 December 2011	65.1	812.3	331.4	–	9.9	309.2	1,073.7	218.8	89.8	2,910.2

Net book value:

At 31 December 2011	73.4	260.1	580.8	–	25.0	867.9	3,182.0	135.3	84.8	5,209.3
At 1 January 2011	68.8	351.7	352.1	–	10.0	722.1	2,987.5	153.5	85.6	4,731.3

Year ended 31 December 2012	Hydro-electric plants £m	Fossil fuel plants £m	Combined cycle plants £m	Wind power plants £m	Gas storage facilities £m	Transmission facilities £m	Distribution facilities £m	Meters and measuring devices £m	Other facilities (see Note (viii)) £m	Total operating plant £m
Cost:										
At 1 January 2012	138.5	1,072.4	912.2	–	34.9	1,177.1	4,255.7	354.1	174.6	8,119.5
Business combinations	–	–	–	1,716.2	–	–	24.4	–	–	1,740.6
Additions	–	2.1	0.8	3.8	0.2	–	34.4	11.5	–	52.8
Transfers from in progress to plant in use	4.2	204.3	36.5	293.3	–	205.8	657.4	–	8.9	1,410.4
Disposals	–	(77.2)	(16.6)	(1.0)	(0.7)	(7.1)	(18.8)	(2.9)	–	(124.3)
At 31 December 2012	142.7	1,201.6	932.9	2,012.3	34.4	1,375.8	4,953.1	362.7	183.5	11,199.0

Depreciation:

At 1 January 2012	65.1	812.3	331.4	–	9.9	309.2	1,073.7	218.8	89.8	2,910.2
Business combinations	–	–	–	362.4	–	–	6.3	–	–	368.7
Charge for the year	4.1	76.0	45.0	72.7	0.7	26.4	99.1	27.7	7.0	358.7
Disposals	–	(77.0)	(13.7)	(1.9)	–	(6.2)	(17.3)	(2.6)	–	(118.7)
At 31 December 2012	69.2	811.3	362.7	433.2	10.6	329.4	1,161.8	243.9	96.8	3,518.9

Net book value:

At 31 December 2012	73.5	390.3	570.2	1,579.1	23.8	1,046.4	3,791.3	118.8	86.7	7,680.1
At 1 January 2012	73.4	260.1	580.8	–	25.0	867.9	3,182.0	135.3	84.8	5,209.3

- (i) Interest on the funding attributable to major capital projects was capitalised during the year at a rate of 1.5% (2011 1.5%). The carrying value of capitalised interest within property, plant and equipment in progress at 31 December 2012 was £27.7 million (2011 £20.0 million).
- (ii) The cost of fully depreciated property, plant and equipment still in use at 31 December 2012 was £776.6 million (2011 £752.0 million).
- (iii) Included within the cost of property, plant and equipment are assets in use not subject to depreciation, being land, of £121.1 million (2011 £112.7 million).
- (iv) The impairment charge of £4.0 million made during the year ended 31 December 2012 was in respect of the cancellation of certain capitalised development projects. The impairment charge of £169.1 million made during the year ended 31 December 2011 comprised a charge of £150.8 million resulting from a reassessment of the operational life of the Longannet coal-fired fuel plant and a charge of £18.3 million resulting from cancellation of capitalised development projects, principally in respect of Carbon Capture.
- (v) During the year ended 31 December 2011, property, plant and equipment with a cost of £9.4 million was transferred by the group to a fellow Iberdrola group company.
- (vi) On 1 January 2012 as part of an Iberdrola group restructuring exercise, ScottishPower acquired certain renewable energy companies from another Iberdrola group company, as set out in Note 34. The cost of property, plant and equipment recognised as part of this business combination under common control, amounted to £2,206.1 million and the related aggregate depreciation amounted to £369.2 million. On 1 July 2011 as part of a group restructuring exercise, the group acquired certain subsidiaries from SPUKH as set out in Note 34. The cost of property, plant and equipment recognised as part of this business combination under common control amounted to £387.4 million and the related aggregate depreciation recognised amounted to £99.8 million.
- (vii) Certain types of plant maintenance stocks were reclassified during the year ended 31 December 2012 as property, plant and equipment to align the presentation of this asset type with that of the Iberdrola group.
- (viii) The 'Other facilities' category of operating plant largely comprises water treatment facilities and Energy Networks communications facilities.
- (ix) Included within 'Other operating income' in the income statement is £14.5 million (2011 £nil) relating to compensation receivable from third parties for items of property, plant and equipment that were impaired, lost or given up.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

8 PROPERTY, PLANT AND EQUIPMENT *continued*

(c) Operating lease arrangements

	2012 £m	2011 £m
(i) Operating lease payments		
Minimum lease payments under operating leases recognised as an expense in the year	16.4	16.8
Contingent based operating lease rents recognised as an expense in the year	42.2	229.1
Sublease payments recognised as an expense in the year	–	0.1
	58.6	246.0

The group leases various property, plant and equipment as a lessee under non-cancellable operating lease arrangements. The leases have varying terms, escalation clauses and renewal rights.

The contingent based operating lease rents primarily relate to contracts under which the group purchases electricity. The expense recognised represents the invoiced amounts under these contracts.

	2012 £m	2011 £m
(ii) Operating lease commitments		
The future minimum lease payments under non-cancellable operating leases are as follows:		
Within one year	16.4	11.6
Between one and five years	38.5	30.1
More than five years	57.8	32.9
	112.7	74.6

The group leases various property, plant and equipment under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

	2012 £m	2011 £m
(iii) Operating lease receivables		
The future minimum lease payments receivable under non-cancellable operating leases are as follows:		
Within one year	5.0	5.4
Between one and five years	7.2	10.5
More than five years	2.2	5.3
	14.4	21.2

The group leases buildings and equipment as a lessor under operating leases. The lease arrangements have initial terms of 1 to 99 years and some contain provisions to extend the term at the option of the lessee. The leases have varying terms, escalation clauses and renewal rights.

Total future minimum non-cancellable sublease rentals expected to be received at 31 December 2012 are £2.1 million (2011 £3.2 million).

(d) Capital commitments

	2012 £m	2011 £m
Contracted but not provided	938.3	327.9

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

9 MEASUREMENT OF FINANCIAL INSTRUMENTS

The table below sets out the carrying amount and fair value of the group's financial instruments:

		2012		2011	
		Carrying Amount £m	Fair Value £m	Carrying Amount £m	Fair Value £m
	Notes				
Financial assets					
Finance lease receivables		2.4	2.4	2.6	2.6
Derivative financial instruments	(a)	336.6	336.6	551.9	551.9
Current receivables	(b)	3,065.6	3,065.6	2,211.7	2,211.7
Other investments		1.8	1.8	1.1	1.1
Cash	(c)	23.3	23.3	9.2	9.2
Short-term deposits	(d)	7.5	7.5	9.5	9.5
Financial liabilities					
Derivative financial instruments	(a)	(357.8)	(357.8)	(513.8)	(513.8)
Loans and other borrowings	(e)	(5,726.6)	(6,078.3)	(3,933.2)	(4,321.9)
Payables	(b)	(1,316.2)	(1,316.2)	(1,367.2)	(1,367.2)

The carrying amount of these financial instruments is calculated as set out in Note 3G. With the exception of loans and other borrowings, the carrying value of financial instruments is a reasonable approximation of fair value. The fair value of loans and other borrowings is calculated as set out in Note (e).

- (a) Further detail on derivative financial instruments is disclosed in Note 19.
- (b) Balances outwith the scope of IFRS 7 have been excluded, namely prepayments, other tax receivables, payments on account and other tax payables.
- (c) Cash is comprised of deposits with banks and other short-term deposits. As a general rule, cash deposited with banks earns interest at rates similar to market rates on daily deposits.
- (d) Short-term deposits mature within a period of less than three months and earn market rates.
- (e) The fair value of listed debt is calculated using the most recently traded price to the year-end date and the fair value of all other loans and borrowings is calculated using a discounted cash flow.

The group holds certain financial instruments which are measured in the balance sheet at fair value. The group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data. This category is comprised of commodity purchase contracts which extend over liquid and illiquid periods. The liquid periods for power and gas within the UK extend to March 2015. Fair values for these contracts have been calculated using forward price curves for illiquid periods which have been developed internally using various models and assumptions that are intended to simulate expected market price levels. Given the proportionately small element of these contracts that falls within the illiquid period, any range of reasonably possible alternative assumptions applied to power and gas prices is unlikely to have a significant impact on contract fair values. For indicative purposes, a 1% increase in commodity prices in the illiquid period would result in approximately £0.4 million impact on reported fair values and a 1% decrease would result in approximately £(0.4) million impact.

	2012				2011			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Fair value of derivative financial instruments								
Assets measured at fair value	–	335.6	1.0	336.6	–	380.6	171.3	551.9
Liabilities measured at fair value	–	(334.8)	(23.0)	(357.8)	–	(451.7)	(62.1)	(513.8)
	–	0.8	(22.0)	(21.2)	–	(71.1)	109.2	38.1

Reconciliation of Level 3 financial assets and liabilities

	Total £m
At 1 January 2011	133.1
Business combinations	31.3
Gains or losses:	
– in income statement credited to Procurements	1.6
Settlements	(56.8)
At 1 January 2012	109.2
Gains or losses:	
– in income statement credited to Procurements	2.5
Settlements	(33.1)
Transfers out of Level 3*	(100.6)
At 31 December 2012	(22.0)

*During the year £100.6 million of Level 3 derivatives were transferred to Level 2 classification due to improved clarification of gas prices as the end of the liquid period approaches.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

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10 INVENTORIES

	Notes	2012 £m	2011 £m
Fuel stocks	(a)	110.6	216.9
Other inventories	(b)	–	11.8
		110.6	228.7

(a) Inventories with a value of £441.8 million (2011 £229.8 million) were recognised as an expense during the year.

(b) During the year, other inventories with a value of £11.7 million (2011 £nil) were transferred to property, plant and equipment (Note 8).

11 TRADE AND OTHER RECEIVABLES

	Notes	2012 £m	2011 £m
Current receivables:			
Receivables due from Iberdrola group companies – trade		88.3	60.2
Receivables due from other Iberdrola group companies – loans	(a)	2,152.7	1,295.8
Receivables due from Iberdrola Finance UK Limited – loans	(b)	85.9	–
Receivables due from Iberdrola group companies – interest		24.6	15.9
Trade receivables and accrued income	(c),(d)	714.1	839.8
Prepayments		30.1	22.4
Other tax receivables		24.4	32.6
		3,120.1	2,266.7
Non-current receivables:			
Prepayments		4.9	–
		4.9	–

(a) Current loans receivable due from other Iberdrola group companies are receivable on demand with interest linked to Base. Base is not expected to change in the short term.

(b) Loans receivable due from Iberdrola Finance UK Limited, a wholly owned subsidiary of Iberdrola S.A., are charged interest at 3 month EURIBOR less 2 basis points and are repayable on demand. A 1% increase in EURIBOR would result in a £0.9 million increase in full year interest receivable.

(c) Trade receivables are stated net of allowance for impairment of doubtful debts of £44.5 million (2011 £54.5 million). Trade receivables are assumed to approximate their fair values due to the short term nature of trade receivables. Provisions for doubtful debts have been estimated by management, taking into account future cash flows, based on prior experience, ageing analysis and an assessment of the current economic environment within which the group operates. The income statement impact on change in bad debt for the year to 31 December 2012 is £38.1 million (2011 £54.9 million).

(d) Amounts due from contract customers included in trade receivables at 31 December 2012 amount to £3.1 million (2011 £6.4 million).

(e) The group enters into standard netting agreements with its commodity trading counterparties in order to mitigate the credit risk exposure of the business. In addition, the group utilises other forms of collateral to manage its credit risk exposure. These forms of collateral include margining for trading with exchanges, cash collateral used for bilateral and brokering trading as well as letters of credit. At 31 December 2012, the group held cash collateral of £39.4 million (2011 £51.8 million) and letters of credit with a value of £27.5 million (2011 £77.5 million) in respect of trade receivables. This cash collateral is included within trade payables.

(f) With the exception of retail customers, the group considers that its credit risk can be considered to be with counterparties in related energy industries or with financial institutions operating in energy markets. The carrying amount of the receivable represents the maximum exposure to credit risk.

(g) Trading terms are governed by Industry Standard agreements which typically provide for interest to be charged where payments are not made on the specified settlement date.

(h) Movements on the provision for impairment of trade receivables are as follows:

	2012 £m	2011 £m
At beginning of year	54.5	73.5
Receivables written off during the year as uncollectible	(48.1)	(73.9)
Provision for receivables impairment	38.1	54.9
At end of year	44.5	54.5

(i) The creation and release of provision for impaired receivables have been included in "Depreciation and amortisation charge, allowances and provisions" in the consolidated income statement (Note 25).

(ii) The provision for impaired receivables mainly relates to Energy Retail customers where a low likelihood of collection has been assessed.

(iii) At 31 December 2012, trade receivables of £57.8 million (2011 £57.2 million) were renegotiated that would otherwise be past due or impaired. These mainly relate to Energy Retail customers who, subsequent to defaulting on original payment terms, have made new arrangements to pay amounts owed.

12 SHARE CAPITAL

	2012 £m	2011 £m
Authorised:		
3,000,000,002 ordinary shares of 50p each (2011 3,000,000,002)	1,500.0	1,500.0
Allotted, called up and fully paid shares:		
1,743,983,102 ordinary shares of 50p each (2011 1,743,983,102)	872.0	872.0

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

13 ANALYSIS OF MOVEMENTS IN EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF SCOTTISH POWER UK PLC

	Ordinary share capital £m	Share premium (Note (a)) £m	Hedge reserve (Note (b)) £m	Other reserves (Note (c)) £m	Retained earnings (Note (d)) £m	Total £m
At 1 January 2011	872.0	398.2	0.8	14.0	777.7	2,062.7
Profit for the year attributable to equity holders of Scottish Power UK plc	–	–	–	–	267.3	267.3
Changes in the value of cash flow hedges	–	–	(87.4)	–	–	(87.4)
Actuarial losses on retirement benefits	–	–	–	–	(112.2)	(112.2)
Tax on items relating to cash flow hedges	–	–	21.9	–	–	21.9
Tax on items relating to actuarial losses on retirement benefits	–	–	–	–	23.4	23.4
Dividends	–	–	–	–	(200.0)	(200.0)
Business combinations (net of tax)	–	–	(7.9)	–	117.8	109.9
At 1 January 2012	872.0	398.2	(72.6)	14.0	874.0	2,085.6
Profit for the year attributable to equity holders of Scottish Power UK plc	–	–	–	–	648.1	648.1
Changes in the value of cash flow hedges	–	–	(11.6)	–	–	(11.6)
Actuarial losses on retirement benefits	–	–	–	–	(351.7)	(351.7)
Tax on items relating to cash flow hedges	–	–	0.2	–	–	0.2
Tax on items relating to actuarial losses on retirement benefits	–	–	–	–	74.0	74.0
Business combinations (net of tax)	–	–	(25.1)	–	1,358.8	1,333.7
At 31 December 2012	872.0	398.2	(109.1)	14.0	2,603.2	3,778.3

(a) The share premium account represents consideration received for shares issued in excess of their nominal amount.

(b) The hedge reserve represents the balance of gains and losses on cash flow hedges (net of taxation) not yet transferred to income or the carrying amount of a non-financial asset. The hedge reserve relating to business combinations in the years ended 31 December 2011 and 31 December 2012 comprise the balances within the hedge reserve as at 1 July 2011 and 1 January 2012 respectively of the companies acquired by the group as part of the corporate restructuring (see Note 34).

(c) Other reserves at 31 December 2012 comprise a revaluation reserve of £5.8 million (2011 £5.8 million), and a capital redemption reserve of £8.2 million (2011 £8.2 million). The revaluation reserve comprises the revaluation of assets arising on the purchase of the remaining 50% of the equity share capital of a former joint venture. The capital redemption reserve comprises the nominal value of the company's ordinary share capital purchased by the company in previous years.

(d) Retained earnings comprise the cumulative balance of profits and losses recognised in the financial statements as adjusted for transactions with shareholders, principally dividends.

(e) The changes in the hedge reserve arising from valuation adjustments to hedging derivatives is set out below:

	Notes	Interest rate swaps £m	Commodity hedges £m	Foreign exchange rate hedges £m	Gross value of hedges £m	Tax effect £m	Total £m
Cash flow hedges							
At 1 January 2011		(0.3)	–	1.4	1.1	(0.3)	0.8
Effective cash flow hedges recognised		–	(170.9)	(2.2)	(173.1)	43.3	(129.8)
De-designated cash flow hedges		–	(0.5)	0.5	–	–	–
Removed from equity and recognised in income statement		0.3	14.6	0.4	15.3	(3.8)	11.5
Removed from equity and recognised in carrying amount of hedged items		–	67.7	2.7	70.4	(17.6)	52.8
Business combinations	(i)	–	(13.6)	3.0	(10.6)	2.7	(7.9)
At 1 January 2012		–	(102.7)	5.8	(96.9)	24.3	(72.6)
Effective cash flow hedges recognised		–	(65.0)	(43.2)	(108.2)	24.9	(83.3)
De-designated cash flow hedges		–	6.2	0.1	6.3	(1.4)	4.9
Removed from equity and recognised in income statement		–	55.3	2.9	58.2	(13.4)	44.8
Removed from equity and recognised in carrying amount of hedged items		–	17.0	15.1	32.1	(7.4)	24.7
Business combinations	(ii)	–	–	(33.5)	(33.5)	8.4	(25.1)
Changes in future tax rates		–	–	–	–	(2.5)	(2.5)
At 31 December 2012		–	(89.2)	(52.8)	(142.0)	32.9	(109.1)

(i) On 1 July 2011 as part of a group restructuring exercise, the group acquired certain subsidiaries from SPUKH as set out in Note 34. The net cash flow hedge reserve recognised as part of this business combination under common control amounted to £7.9 million.

(ii) On 1 January 2012, as part of an Iberdrola group reorganisation, the group acquired certain renewable energy companies from another Iberdrola group company, as set out at Note 34. The net cash flow hedge reserve recognised as part of this business combination under common control amounted to £25.1 million.

(iii) The maturity analysis of amounts included in the hedge reserve is as follows:

	2012 £m	2011 £m
Less than 1 year	(90.8)	(41.9)
1-2 years	(14.8)	(26.9)
2-3 years	(2.6)	(3.2)
3-4 years	(0.9)	(0.6)
	(109.1)	(72.6)

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

14 NON-CONTROLLING INTERESTS

	Note	£m
At 1 January 2011 and 1 January 2012		–
Business combinations	(a)	0.3
Net profit attributable to non-controlling interests		0.1
Dividends paid to non-controlling interests		(0.2)
At 31 December 2012		0.2

(a) On 1 January 2012, as part of an Iberdrola group reorganisation, the group acquired certain renewable energy companies from another Iberdrola group company, as set out at Note 34. Non-controlling interests recognised as part of this business combination under common control, amounted to £0.3 million.

15 DEFERRED INCOME

	At 1 January 2011 £m	Business combinations (Note (a)) £m	Receivable during year £m	Released to income statement £m	At 31 December 2011 £m
Year ended 31 December 2011					
Capital grants	8.9	–	5.0	(11.3)	2.6
Transfer of assets from customers	668.5	–	75.8	(20.9)	723.4
Emissions allowances allocated	–	6.1	111.6	(117.7)	–
Other revenue-related deferred income	1.2	–	2.7	(1.2)	2.7
Total deferred income	678.6	6.1	195.1	(151.1)	728.7
	At 1 January 2012 £m	Business combinations (Note (a)) £m	Receivable during year £m	Released to income statement £m	At 31 December 2012 £m
Year ended 31 December 2012					
Capital grants	2.6	2.2	–	(0.7)	4.1
Transfer of assets from customers	723.4	–	100.4	(23.8)	800.0
Emissions allowances allocated	–	–	56.1	(56.1)	–
Other revenue-related deferred income	2.7	–	–	(2.7)	–
Total deferred income	728.7	2.2	156.5	(83.3)	804.1

(a) On 1 July 2011, as part of a group restructuring exercise, the group acquired certain subsidiaries from SPUKH as set out at Note 34. Deferred income recognised as part of this business combination under common control, amounted to £6.1 million. On 1 January 2012, as part of an Iberdrola group reorganisation exercise, the group acquired certain renewable energy companies from another Iberdrola group company, as set out at Note 34. Deferred income recognised as part of this business combination under common control, amounted to £2.2 million.

16 RETIREMENT BENEFIT OBLIGATIONS

(a) Analysis of balance

The amounts recognised in the balance sheet in respect of retirement benefit obligations are detailed below:

	2012 £m	2011 £m
Non-current liabilities	498.7	212.1

(b) Group pension arrangements

ScottishPower operates the following pension schemes for staff:

Scheme	Scottish Power Pension Scheme ('SPPS')	Manweb Group of Electricity Supply Pension Scheme ('Manweb')	Stakeholder Pension Plan
Type of benefit	Final salary	Final salary	Defined contribution
New entrants	No*	No	Yes
Funded separately from group assets	Yes	Yes	Yes
Administration method	Trustee board	Trustee board	Insurance contract
Member contributions	5% of salary	5.5% of salary	5% of salary
Group contributions – how determined	Agreement of trustees and group following actuarial valuation (last valuation: 31 March 2009)**	Agreement of trustees and group following actuarial valuation (last valuation: 31 March 2009)**	Defined
Current actual group contributions	21.8% of salary	23.3% of salary	Service-related, 6% to 14% of salary
Special contributions during year ended 31 December 2012	£12.8 million	£25.4 million	None
Special contributions planned for year ending 31 December 2013	£13.1 million	£26.0 million	None
Pension charge	Based on advice of independent qualified actuary	Based on advice of independent qualified actuary	Equal to actual group contributions in the year

*After 10 years' membership of the Stakeholder Pension Plan certain members will be offered access to defined benefits for future service.

**The 31 March 2012 valuation is currently ongoing and it is expected to be completed by 30 June 2013.

The age profile of the two final salary schemes is expected to rise over time, due to the reduction in new entrants. This will in turn result in increasing service costs for these two schemes due to the actuarial valuation method used (the projected unit method). The group believes that the projected unit method continues to be appropriate at present, and provides a reasonable basis for assessing the group's final salary pension costs.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

16 RETIREMENT BENEFIT OBLIGATIONS *continued*

(b) Group pension arrangements *continued*

Investment strategies

Each of the pension schemes is invested in an appropriately diversified range of assets. The broad proportions of each asset class in which the schemes aim to be invested are as follows, however it is important to note that this may vary from time to time as markets change and as cash may be held for strategic reasons.

	ScottishPower 2012	Manweb 2012	ScottishPower 2011	Manweb 2011
Equities	22%	25%	32%	40%
Infrastructure	6%	5%	5%	4%
Liability driven investment	50%	50%	57%	55%
Property	6%	–	5%	–
Diversified growth fund	10%	20%	–	–
Mezzanine debt	6%	–	–	–
Cash	–	–	1%	1%
Total	100%	100%	100%	100%

At 31 December 2012 no scheme held ScottishPower or Iberdrola shares (2011 none).

Additional pension arrangement

The group also operates an Unfunded Unapproved Retirement Benefit Scheme ("UURBS") for former senior executives' benefit promises in excess of limits set by the UK taxation authorities. The UURBS has no invested assets, and the group has provided £6.1 million as at 31 December 2012 (2011 £5.1 million) for the benefit promises which will ultimately be paid by the group.

(c) Pensions – defined contribution scheme

The charge for the year ended 31 December 2012 in respect of the Stakeholder Pension Plan is £2.9 million (2011 £2.0 million).

(d) Pensions – defined benefit schemes

The group operates defined benefit pension schemes as described earlier in this note. Formal actuarial valuations were carried out as described earlier and updated to 31 December 2012 by a qualified independent actuary. The major assumptions applied by the actuary are given in footnote (e).

(i) Analysis of net liability relating to pensions

	2012				2011			
	SPPS £m	Manweb £m	UURBS £m	Total £m	SPPS £m	Manweb £m	UURBS £m	Total £m
Present value of funded obligations	(2,881.2)	(1,153.5)	–	(4,034.7)	(2,492.1)	(988.0)	–	(3,480.1)
Fair value of scheme assets	2,627.4	914.7	–	3,542.1	2,447.6	825.5	–	3,273.1
Net liability of funded plans	(253.8)	(238.8)	–	(492.6)	(44.5)	(162.5)	–	(207.0)
Present value of unfunded obligations	–	–	(6.1)	(6.1)	–	–	(5.1)	(5.1)
Net liability	(253.8)	(238.8)	(6.1)	(498.7)	(44.5)	(162.5)	(5.1)	(212.1)

Amounts in the balance sheet:

Non-current liabilities	(253.8)	(238.8)	(6.1)	(498.7)	(44.5)	(162.5)	(5.1)	(212.1)
Net liability	(253.8)	(238.8)	(6.1)	(498.7)	(44.5)	(162.5)	(5.1)	(212.1)

(ii) The amounts recognised are as follows:

	2012				2011			
	SPPS £m	Manweb £m	UURBS £m	Total £m	SPPS £m	Manweb £m	UURBS £m	Total £m
Current service cost	35.9	11.0	–	46.9	35.2	10.4	–	45.6
Interest on obligation	115.8	45.7	0.3	161.8	123.3	49.6	0.2	173.1
Expected return on scheme assets	(145.6)	(49.6)	–	(195.2)	(139.9)	(49.5)	–	(189.4)
Past service cost	9.8	0.4	0.5	10.7	5.4	2.1	1.1	8.6
Total income statement charge*	15.9	7.5	0.8	24.2	24.0	12.6	1.3	37.9
Actual return on scheme assets	228.3	90.8	–	319.1	122.6	(4.5)	–	118.1
Net actuarial losses recognised in the Consolidated Statement of Comprehensive Income	(243.4)	(107.8)	(0.5)	(351.7)	(54.3)	(57.6)	(0.3)	(112.2)

* The amounts above are stated before capitalisation of employee costs relating to self-constructed assets.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

16 RETIREMENT BENEFIT OBLIGATIONS *continued*

(d) Pensions-defined benefit schemes *continued*

(iii) Changes in the present value of the defined benefit obligations are as follows:

	SPPS 2012 £m	Manweb 2012 £m	UURBS 2012 £m	Total 2012 £m	SPPS 2011 £m	Manweb 2011 £m	UURBS 2011 £m	Total 2011 £m
Defined benefit obligation at beginning of year	2,492.1	988.0	5.1	3,485.2	2,379.5	962.3	3.7	3,345.5
Current service cost	35.9	11.0	–	46.9	35.2	10.4	–	45.6
Interest on obligation	115.8	45.7	0.3	161.8	123.3	49.6	0.2	173.1
Scheme members' contributions	8.0	2.4	–	10.4	8.3	2.7	–	11.0
Past service costs	9.8	0.4	0.5	10.7	5.4	2.1	1.1	8.6
Actuarial losses	326.1	149.0	0.5	475.6	37.0	3.6	0.3	40.9
Benefits paid	(106.5)	(43.0)	(0.3)	(149.8)	(96.6)	(42.7)	(0.2)	(139.5)
Defined benefit obligation at end of year	2,881.2	1,153.5	6.1	4,040.8	2,492.1	988.0	5.1	3,485.2
Analysis of defined benefit obligation								
Plans that are wholly or partly funded	2,881.2	1,153.5	–	4,034.7	2,492.1	988.0	–	3,480.1
Plans that are wholly unfunded	–	–	6.1	6.1	–	–	5.1	5.1
Total	2,881.2	1,153.5	6.1	4,040.8	2,492.1	988.0	5.1	3,485.2

(iv) Changes in the fair value of scheme assets are as follows:

	SPPS 2012 £m	Manweb 2012 £m	UURBS 2012 £m	Total 2012 £m	SPPS 2011 £m	Manweb 2011 £m	UURBS 2011 £m	Total 2011 £m
Fair value of scheme assets at beginning of year	2,447.6	825.5	–	3,273.1	2,357.9	826.8	–	3,184.7
Expected return on scheme assets	145.6	49.6	–	195.2	139.9	49.5	–	189.4
Actuarial gains/(losses)	82.7	41.2	–	123.9	(17.3)	(54.0)	–	(71.3)
Employer contributions	50.0	39.0	0.3	89.3	55.4	43.2	0.2	98.8
Scheme members' contributions	8.0	2.4	–	10.4	8.3	2.7	–	11.0
Benefits paid	(106.5)	(43.0)	(0.3)	(149.8)	(96.6)	(42.7)	(0.2)	(139.5)
Fair value of scheme assets at end of year	2,627.4	914.7	–	3,542.1	2,447.6	825.5	–	3,273.1

(e) Actuarial assumptions

(i) The major assumptions used by the actuary for the pensions arrangements, for all schemes were as follows and are expressed as weighted averages:

	2012	2011
Rate of increase in salaries	4.4% p.a.	4.5% p.a.
Rate of increase in deferred pensions	2.9% p.a.	3.0% p.a.
Rate of increase in pensions in payment	2.9% p.a.	2.9% p.a.
Discount rate	4.2% p.a.	4.7% p.a.
Inflation assumption	2.9% p.a.	3.0% p.a.

The discount rate is a critical assumption in determining the group's defined benefit obligation. As at 31 December 2012, if the discount rate were to be increased/decreased by 0.25% the group's defined benefit obligation would be reduced/increased by £172.1 million (2011 £146.3 million), respectively.

(ii) The weighted average life expectancy for mortality used to determine the benefit obligations were as follows:

	SPPS	2012 Manweb	UURBS	SPPS	2011 Manweb	UURBS
Member age 63 (current life expectancy)						
Male	24.8	24.8	24.8	22.2	22.2	22.2
Female	26.8	26.8	26.8	25.9	25.9	25.9
Member age 45 (life expectancy at age 63)						
Male	26.2	26.2	26.2	23.9	23.9	23.9
Female	28.4	28.4	28.4	26.9	26.9	26.9

The mortality assumptions are critical assumptions in determining the group's defined benefit obligation. As at 31 December 2012, if it were to be assumed that the members live one year longer than the assumptions above, the group's defined benefit obligation would be increased by £118.9 million (2011 £105.9 million).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

16 RETIREMENT BENEFIT OBLIGATIONS *continued*

(e) Actuarial assumptions *continued*

(iii) Allowance for cash commutation

Within the pension schemes, members are assumed to commute 25% of their benefits for a tax-free cash sum where this option is available.

(iv) The weighted average asset allocations were as follows:

	Asset allocations			
	2012		2011	
	SPPS	Manweb	SPPS	Manweb
Equities	35.1%	41.8%	32.0%	40.2%
Infrastructure	5.2%	4.5%	5.0%	4.4%
Liability driven investment	47.8%	52.7%	57.0%	54.8%
Property	4.8%	–	5.1%	–
Cash	0.9%	1.0%	0.9%	0.6%
Mezzanine debt	1.3%	–	–	–
Diversified growth funds	4.9%	–	–	–

The expected returns on each asset class for SPPS and Manweb were as follows:

	Long-term rates of return expected	
	2012	2011
Equities	8.3% p.a.	8.3% p.a.
Infrastructure	7.1% p.a.	7.1% p.a.
Liability driven investment	3.8% p.a.	3.8% p.a.
Property	7.4% p.a.	7.4% p.a.
Cash	2.2% p.a.	2.2% p.a.
Mezzanine debt	7.6% p.a.	–
Diversified growth funds	7.6% p.a.	–
Expected return on scheme assets	5.8% p.a.	6.0% p.a.

The long-term rates of return have for 31 December 2012 been derived as follows:

- Equities: the long-term UK Government fixed interest stock yield, plus 5.9% p.a.
- Infrastructure: the long-term UK Government fixed interest stock yield, plus 4.7% p.a.
- Liability driven investment: the long-term UK Government fixed interest stock yield, plus 1.4% p.a.
- Property: the long-term UK Government fixed interest stock yield, plus 5.0% p.a.
- Mezzanine debt: the long-term UK Government fixed interest stock yield plus 5.2% p.a.
- Diversified growth funds: the long-term UK Government fixed interest stock yield plus 5.2% p.a.

In all cases, for IAS 19 reporting purposes the long-term rates of return have been reduced by 0.3% p.a. (2011 0.3% p.a.) to reflect scheme expenses to arrive at the figures shown above. These return assumptions are based on both historical performance and independent advisors' forward-looking views of the financial markets.

(f) History of experience gains and losses

(i) The amounts for the current year and previous periods in relation to the defined benefit plans are given below:

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m	Year ended 31 December 2008 £m
Defined benefit pension schemes					
Difference between expected and actual return on scheme assets:					
– amount	123.9	(71.3)	115.6	200.6	(400.3)
– percentage of scheme assets	4%	(2)%	4%	7%	(15)%
Experience gains and losses on scheme liabilities:					
– amount	(36.5)	(17.5)	(17.7)	(23.2)	(10.4)
– percentage of scheme liabilities	1%	1%	0%	1%	0%
Present value of defined benefit obligations	(4,040.8)	(3,485.2)	(3,345.5)	(3,060.4)	(2,495.7)
Fair value of plan assets	3,542.1	3,273.1	3,184.7	2,941.1	2,659.6
(Deficit)/surplus in defined benefit plans	(498.7)	(212.1)	(160.8)	(119.3)	163.9

The cumulative loss recognised in the Statement of Comprehensive Income in respect of pensions since 1 April 2004 amounts to £699.7 million.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

16 RETIREMENT BENEFIT OBLIGATIONS *continued*

(f) History of experience gains and losses *continued*

(iii) The amounts for the current and previous year in relation to the individual defined benefit plans are given below:

	SPPS 2012 £m	Manweb 2012 £m	UURBS 2012 £m	Total 2012 £m	SPPS 2011 £m	Manweb 2011 £m	UURBS 2011 £m	Total 2011 £m
Difference between expected and actual return on scheme assets								
– amount	82.7	41.2	–	123.9	(17.3)	(54.0)	–	(71.3)
– percentage of scheme assets	3%	5%	–	4%	(1)%	(7)%	–	(2)%
Experience gains and losses on scheme liabilities								
– amount	(15.8)	(20.6)	(0.1)	(36.5)	(4.4)	(13.3)	0.2	(17.5)
– percentage of scheme liabilities	1%	2%	2%	1%	0%	1%	(4)%	1%
Present value of defined benefit obligations	(2,881.2)	(1,153.5)	(6.1)	(4,040.8)	(2,492.1)	(988.0)	(5.1)	(3,485.2)
Fair value of plan assets	2,627.4	914.7	–	3,542.1	2,447.6	825.5	–	3,273.1
Deficit in defined benefit plans	(253.8)	(238.8)	(6.1)	(498.7)	(44.5)	(162.5)	(5.1)	(212.1)

(g) Future contributions

The group expects to contribute £80.0 million to the pension schemes in the year ending 31 December 2013 based on the agreement with scheme trustees following the valuation at March 2009. The March 2012 valuation is due to conclude by 30 June 2013 and may result in different levels of contribution for 2013. The expected contributions split by scheme are as follows: SPPS £43.0 million, Manweb £37.0 million and UURBS Enil.

17 OTHER PROVISIONS

	Notes	At 1 January 2011 £m	New provisions £m	Business combinations (note (h)) £m	Unwinding of discount £m	Utilised during year £m	Released during year £m	At 31 December 2011 £m
Year ended 31 December 2011								
Reorganisation and restructuring	(a)	5.3	6.0	–	–	(3.5)	(1.9)	5.9
Decommissioning and environmental	(b)	70.6	5.0	1.7	1.6	(5.0)	–	73.9
Emissions allowances	(c)	184.2	98.0	49.1	–	(185.5)	–	145.8
Onerous contracts	(d)	22.3	–	–	0.7	(1.9)	–	21.1
Insurance	(e)	10.3	1.1	–	–	(1.7)	(0.4)	9.3
Regulatory	(f)	–	21.5	–	–	–	–	21.5
Other	(g)	2.9	5.5	–	–	(2.1)	(0.1)	6.2
		295.6	137.1	50.8	2.3	(199.7)	(2.4)	283.7

	Notes	At 1 January 2012 £m	Business combinations (note (h)) £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	Transfers from creditors £m	Released during year £m	At 31 December 2012 £m
Year ended 31 December 2012									
Reorganisation and restructuring	(a)	5.9	–	4.7	–	(5.2)	–	(1.8)	3.6
Decommissioning and environmental	(b)	73.9	35.6	2.3	2.2	(2.2)	–	–	111.8
Emissions allowances	(c)	145.8	–	63.4	–	(144.3)	–	–	64.9
Onerous contracts	(d)	21.1	–	–	0.3	(3.2)	–	(0.8)	17.4
Insurance	(e)	9.3	–	1.0	–	(1.2)	6.9	(1.1)	14.9
Regulatory	(f)	21.5	–	9.0	–	(0.8)	–	–	29.7
Other	(g)	6.2	5.9	4.2	–	(3.1)	–	(0.2)	13.0
		283.7	41.5	84.6	2.5	(160.0)	6.9	(3.9)	255.3

Analysis of total other provisions

	2012 £m	2011 £m
Current	138.3	196.3
Non-current	117.0	87.4
	255.3	283.7

- (a) The provision for reorganisation and restructuring principally relates to restructuring within the Energy Retail, Energy Wholesale and corporate office functions. This provision is expected to be utilised during 2013.
- (b) The provision for decommissioning and environmental costs is the discounted future estimated costs of decommissioning the group's power plants (including wind farms) and the obligation to remove asbestos from power stations over the course of their operational lives. The decommissioning of these plants is expected to occur over the period between 2013 and 2042.
- (c) The provision for emissions allowances represents the value of emissions allowances certificates expected to be delivered in 2013.
- (d) The provision for onerous contracts relates to retail property leases. The leases will expire over the period between 2013 and 2025.
- (e) The provision for insurance principally represents the value of claims reserves.
- (f) The provision for regulatory costs relates to various contractual obligations and the future costs associated with various regulatory reviews. The reviews are expected to be concluded in 2013.
- (g) The 'Other' category comprises provisions which are not individually sufficiently material to warrant separate disclosure.
- (h) On 1 July 2011, as part of a group restructuring exercise, the group acquired certain subsidiaries from SPUKH as set out at Note 34. Provisions recognised as part of this business combination under common control, amounted to £50.8 million. On 1 January 2012, as part of an Iberdrola group reorganisation exercise, the group acquired certain renewable energy companies from another Iberdrola group company, as set out in Note 34. Provisions recognised as part of this business combination under common control, amounted to £41.5 million.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

18 LOANS AND OTHER BORROWINGS

Analysis by instrument and maturity	Notes	Interest rate*	Maturity	2012 £m	2011 £m
On demand loans with Iberdrola group companies		Base +1%	On demand	3,361.4	2,002.8
Bank overdraft		Base +1%	On demand	0.1	0.7
Collateral		LIBOR	30 June 2013	39.1	47.9
£200 million euro-sterling bond	(b),(c)	8.375%	20 February 2017	199.4	199.2
Long-term loans with Iberdrola group companies		LIBOR + 0.34%	17 December 2018	150.0	150.0
Long-term loans with Iberdrola group companies		3.858%	29 January 2019	150.0	150.0
£300 million medium-term note	(d)	5.9%	22 February 2021	294.6	293.9
Loans with Iberdrola group companies		EURIBOR + 1.025%	30 May 2022	107.1	–
£250 million euro-sterling bond	(b),(e)	6.75%	29 May 2023	248.2	248.1
£175 million inflation linked bond	(d)	3.494% x RPI	13 October 2024	252.0	243.8
£350 million euro-sterling bond	(b),(f)	5.875%	17 July 2026	346.1	345.8
£350 million euro-sterling bond	(b),(g)	4.875%	20 September 2027	345.2	–
10 billion JPY loan	(h)	4.6%	27 July 2029	83.4	101.0
£50 million medium-term note	(d)	5.75%	9 December 2039	50.0	50.0
£100 million medium-term note	(d)	6.375%	31 May 2041	100.0	100.0
				5,726.6	3,933.2

*Base - Bank of England Base Rate; LIBOR - London Inter-Bank Offer Rate; EURIBOR – Euro Bank Offered Rate; RPI - Retail Prices Index; JPY–Japanese Yen

Analysis of total loans and other borrowings	Note	2012 £m	2011 £m
Non-current		2,328.8	1,884.3
Current	(a)	3,397.8	2,048.9
		5,726.6	3,933.2

- (a) Current borrowings comprise loans with Iberdrola group companies repayable on demand, bank overdrafts and collateral together with finance costs due to be amortised within one year, the short term element of fair value hedge adjustments and the adjustments on discontinued fair value hedges due to be amortised within one year. This totalled £(2.8) million (2011 £(2.5) million).
- (b) These bonds contain a “Loss of licences” covenant that will require repayment of the outstanding amount should the group lose all of its electricity licences (distribution, transmission and supply licences).
- (c) The Sterling Bond due 2017 can be redeemed at any time by the group at the higher of principal amount or redemption price (as determined by HSBC bank plc) giving 30 to 90 days’ notice to lender.
- (d) Scottish Power Limited and the company have an established joint US\$7 billion euro-medium term note programme. Scottish Power Limited has not issued under the programme. The company has in issue various notes in Sterling which can be redeemed by the company with 30 to 90 days’ notice in case of unfavourable and unavoidable changes in the UK tax laws impacting on the note payments.
- (e) The Sterling bond due 2023 can be redeemed at any time by the group at the higher of principal amount or redemption price (as determined by HSBC Bank plc) giving 30 to 45 days’ notice to the lender.
- (f) The £350 million euro-sterling bond will be redeemed at its principal amount on 17 July 2026 unless previously redeemed or purchased and cancelled. The bond can be redeemed at any time by the group at a higher redemption price (as determined by a financial advisor appointed by the group and Guarantor) giving 30 to 60 days’ notice.
- (g) The £350 million euro-sterling bond will be redeemed at its principle amount on 20 September 2027 unless previously redeemed or purchased and cancelled. The bond can be redeemed at any time by the group at a higher redemption price (as determined by a financial advisor appointed by the group and Guarantor) giving 30 to 60 days’ notice.
- (h) The interest rate quoted above on the 10 billion JPY loan is fixed. This is changed to a variable rate by a cross currency swap.
- (i) The group has no undrawn committed borrowing facilities at 31 December 2012 (2011 £nil).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

19 DERIVATIVE FINANCIAL INSTRUMENTS

Analysis of derivative financial instruments – carrying value

	2012				2011			
	Assets		Liabilities		Assets		Liabilities	
	Current	Non-current	Current	Non-current	Current	Non-current	Current	Non-current
Hedging derivatives								
Exchange rate hedges								
Fair value hedge								
– Currency swap	0.7	32.7	–	–	0.7	50.3	–	–
Cash flow hedge								
– Foreign exchange rate	4.8	0.6	(45.3)	(14.5)	15.5	4.1	(18.1)	(3.3)
Commodity hedge								
Cashflow hedge	22.0	2.2	(69.3)	(10.6)	12.6	5.3	(61.9)	(42.2)
Non-hedging derivatives								
Exchange rate derivative								
– Foreign exchange rate	4.2	0.6	(4.4)	(0.9)	14.4	1.7	(10.6)	(1.9)
Commodity derivatives	185.7	83.1	(178.0)	(34.8)	288.8	158.5	(297.1)	(78.7)
Total derivatives	217.4	119.2	(297.0)	(60.8)	332.0	219.9	(387.7)	(126.1)

20 EFFECT OF HEDGING AND DERIVATIVE INSTRUMENTS ON THE RESULTS

An analysis of the effect of hedging and derivative financial instruments on the income statement is given below:

	Notes	2012 £m	2011 £m
Operating derivatives:			
Effect of commodity derivative instruments	(a)	(4.6)	(78.4)
Financing derivatives:			
Effect of financing derivatives	(a)	(3.8)	20.1
Fair value hedges:			
Movements in the fair value of hedging instruments		(4.9)	8.7
Movements in the fair value of hedged item		4.9	(8.5)
Effect of fair value hedges		–	0.2
Cash flow hedge – amounts released from equity:			
Commodities		(55.3)	(14.6)
Financing		(2.9)	(0.7)
Effect of cash flow hedges	(b)	(58.2)	(15.3)
Total	(c)	(66.6)	(73.4)

(a) The amount includes de-designated cash flow hedges.

(b) The amount relates to gains and losses on the effective portions of cash flow hedges which have previously been deferred in equity which have been transferred to the income statement in the current year to match timing of occurrence of the hedged cash flows or where hedged forecasted cash flows are no longer expected to occur.

(c) The net effect of hedging and derivative financial instruments with Iberdrola group companies on the income statement for the year ended 31 December 2012 was £(3.9) million (2011 £0.4 million).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

21 TRADE AND OTHER PAYABLES

	Note	2012 £m	2011 £m
Current trade and other payables:			
Payables due to Iberdrola group companies – trade		184.3	220.0
Payables due to Iberdrola group companies – capital		11.2	–
Payables due to Iberdrola group companies – interest		26.0	32.9
Trade payables	(a)	782.7	716.8
Other taxes and social security		15.4	14.1
Payments received on account		133.9	117.2
Capital payables and accounts		230.8	173.5
Other payables		75.1	220.2
		1,459.4	1,494.7
Non-current other payables:			
Payments received on account		–	1.1
Other payables		6.1	3.8
		6.1	4.9

(a) Trade payables include amounts due on commodity activities.

(b) At 31 December 2012 the group posted amounts of cash collateral of £49.6 million (2011 £13.2 million). These amounts are included within trade receivables in Note 11. In addition the group has issued letters of credit of £67.4 million (2011 £14.8 million).

22 DEFERRED TAX

Deferred tax provided in the Accounts is as follows:

	Note	Property, plant and equipment £m	Derivative financial instruments £m	Retirement benefits £m	Other temporary differences £m	Total £m
At 1 January 2011						
Business combinations	(c)	20.5	5.4	–	–	25.9
(Credit)/charge to income statement		(55.6)	(18.3)	14.7	20.8	(38.4)
Recorded in the statement of comprehensive income		–	(21.9)	(23.4)	–	(45.3)
At 1 January 2012						
Business combinations	(c)	280.9	(8.4)	–	124.7	397.2
(Credit)/charge to income statement		(42.5)	(7.1)	14.1	(12.6)	(48.1)
Recorded in the statement of comprehensive income		–	(0.2)	(74.0)	–	(74.2)
At 31 December 2012						
		836.9	(22.3)	(116.2)	102.0	800.4

(a) At 31 December 2012, the group had unutilised capital losses of £18.7 million (2011 £19.4 million). No deferred tax asset has been recognised in the accounts due to the unpredictability of suitable future profit streams against which these losses may be utilised.

(b) The government has announced that it intends to reduce the rate of UK corporation tax to 20% by 1 April 2015. The rate of corporation tax reduced from 28% to 26% on 1 April 2011 and to 24% on 1 April 2012. A further reduction to 23%, effective from 1 April 2013, was enacted at the balance date. These changes have reduced the tax rate expected to apply when temporary differences reverse.

Reductions of another 3% are expected and will reduce the property, plant and equipment element of the deferred tax provision. The estimated impact of these changes will be a reduction of £109.2 million. It is not possible to quantify the impact of the rate reduction on the other elements of the deferred tax balance.

(c) On 1 July 2011, as part of a group restructuring exercise, the group acquired certain subsidiaries from Scottish Power UK Holdings Limited as set out at Note 34. Deferred tax liabilities recognised as part of this business combination amounted to £25.9 million. On 1 January 2012, as part of an Iberdrola restructuring exercise, the group acquired certain renewable energy companies from another Iberdrola group company as set out in Note 34. Deferred tax recognised as part of this business combination under common control amounted to £397.2 million.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

23 EMPLOYEE INFORMATION

(a) Staff costs

	2012 £m	2011 £m
Wages and salaries	281.8	269.1
Social security costs	25.3	24.4
Pension and other costs	69.2	64.3
Total staff costs	376.3	357.8
Less: capitalised staff costs	(122.2)	(105.5)
Charged to the income statement	254.1	252.3

(b) Employee numbers

The year end and average numbers of employees (full and part-time) employed by the group, including executive directors, were:

	Year end 2012	Average 2012	Year end 2011	Average 2011
United Kingdom				
Energy Networks	2,797	2,723	2,693	2,708
Energy Wholesale	754	784	850	783
Energy Retail	2,685	2,952	3,256	3,490
Renewables	239	229	–	–
Corporate	715	718	719	740
Total	7,190	7,406	7,518	7,721

The year end and average numbers of full-time equivalent staff employed by the group, including executive directors, were:

	Year end 2012	Average 2012	Year end 2011	Average 2011
Total	6,891	7,085	7,166	7,355

24 TAXES OTHER THAN INCOME TAX

	Note	2012 £m	2011 £m
Property taxes		105.6	91.8
Business taxes		1.3	1.3
Other taxes	(a)	180.4	76.9
		287.3	170.0

(a) Other taxes mainly comprise obligations specific to the energy industry such as CERT, CESP and WHD (see Directors Report).

25 DEPRECIATION AND AMORTISATION CHARGE, ALLOWANCES AND PROVISIONS

	2012 £m	2011 £m
Property, plant and equipment depreciation charge	369.2	274.4
Intangible asset amortisation	37.7	35.6
Capital grants transferred to income for the year	(0.7)	(11.3)
Charges and provisions, allowances and impairment of assets	28.4	245.3
	434.6	544.0

26 FINANCE INCOME

	2012 £m	2011 £m
Interest on bank and other deposits	0.8	0.9
Interest receivable from Iberdrola group companies	25.2	16.5
Gain on sale of other investments	–	9.6
Foreign exchange gains	8.6	2.0
Expected return on retirement benefit assets	136.6	132.6
Fair value and other gains on financing derivatives	19.7	22.6
	190.9	184.2

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

27 FINANCE COSTS

	Note	2012 £m	2011 £m
Interest on bank loans and overdrafts		0.3	0.7
Interest on amounts due to Iberdrola group companies		54.2	29.2
Interest on other borrowings		109.1	104.6
Unwinding of discount on provisions		2.5	2.3
Foreign exchange losses		11.1	1.8
Interest on retirement benefit obligations		113.2	121.2
Fair value and other losses on financing derivatives		23.5	2.3
		313.9	262.1
Capitalised interest	(a)	(7.7)	(3.0)
		306.2	259.1

(a) The tax relief on the capitalised interest for the year ended 31 December 2012 was £1.9 million (2011 £0.9 million).

28 INCOME TAX

	2012 £m	2011 £m
Current tax:		
UK Corporation tax	151.8	88.5
Adjustments in respect of prior periods	(10.2)	(22.6)
Current tax for the year	141.6	65.9
Deferred tax:		
Origination and reversal of temporary differences	38.5	0.9
Adjustments in respect of prior years	(1.1)	11.1
Impact of tax rate change	(85.5)	(50.4)
Deferred tax for the year	(48.1)	(38.4)
Income tax expense for the year	93.5	27.5

The tax charge on profit before tax for the year varied from the standard rate of UK Corporation tax applicable to group companies as follows:

	2012 £m	2011 £m
Corporation tax at 24.5% (2011 26.5%)	181.7	78.1
Adjustments in respect of prior years	(11.3)	(11.5)
Impact of tax rate change	(85.5)	(50.4)
Other permanent differences	8.6	11.3
Income tax expense for the year	93.5	27.5

29 DIVIDENDS

	2012 pence per ordinary share	2011 pence per ordinary share	2012 £m	2011 £m
Interim dividend paid	–	11.5	–	200.0

30 CONTINGENT LIABILITIES

Legal proceedings

The group's businesses are parties to various legal claims, actions and complaints, certain of which may involve material amounts. Although the group is unable to predict with certainty whether or not it will ultimately be successful in these legal proceedings or, if not, what the impact might be, the company currently believes that disposition of these matters will not have a materially adverse effect on the group's consolidated Accounts.

31 FINANCIAL COMMITMENTS

Contractual commitments

The group manages its energy resource requirements by integrating long-term firm, short-term and spot market purchases with its own generating resources to manage volume and price volatility and maximise value across the energy value chain. As part of its energy resource portfolio the group is committed under long-term purchase contracts summarised in the table below.

	2012						Total £m
	2013 £m	2014 £m	2015 £m	2016 £m	2017 £m	2018 and thereafter £m	
Long-term energy purchase contract commitments	5,179.1	1,072.9	463.7	266.1	86.5	–	7,068.3
Other contractual commitments	141.9	56.1	20.3	14.1	10.5	32.2	275.1

	2011						Total £m
	2012 £m	2013 £m	2014 £m	2015 £m	2016 £m	2017 and thereafter £m	
Long-term energy purchase contract commitments	5,944.6	1,704.4	545.8	411.9	315.7	91.4	9,013.8
Other contractual commitments	87.4	12.0	3.3	0.2	0.1	–	103.0

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

32 RELATED PARTY TRANSACTIONS

(a) Transactions and balances arising in the normal course of business

	2012					2011				
	Ultimate parent (Iberdrola S.A.) £m	Ultimate UK parent (Scottish Power Limited) £m	Immediate parent (Scottish Power UK Holdings Limited) £m	Other Iberdrola group companies £m	Jointly controlled entities £m	Ultimate parent (Iberdrola S.A.) £m	Ultimate UK parent (Scottish Power Limited) £m	Immediate parent (Scottish Power UK Holdings Limited) £m	Other Iberdrola group companies £m	Jointly controlled entities £m
Types of transaction										
Sales and rendering of services	17.8	1.0	–	166.5	2.2	10.4	–	–	832.1	2.2
Purchases and receipt of services	(39.7)	(5.0)	(0.7)	(458.4)	(1.2)	(35.3)	(6.8)	(0.7)	(2,257.1)	(5.0)
Finance income – loans	–	24.7	–	0.5	–	–	16.5	–	–	0.1
Finance costs – loans	(2.7)	(42.9)	–	(8.6)	(0.1)	(0.1)	(29.1)	–	–	–
Net gains/(losses) on foreign exchange	0.8	0.1	–	(1.5)	–	(0.1)	–	–	–	–
Net gains on financing derivatives	–	(3.8)	–	–	–	–	0.9	–	–	–
Dividends paid	–	–	–	–	–	–	–	(200.0)	–	–
Transfer of intangibles	(138.5)	–	–	–	–	–	–	–	–	–
Business combinations (note (iii))	–	–	–	(27.8)	–	–	–	(65.3)	–	–
Balances outstanding										
Loans receivable	–	2,152.7	–	85.9	1.5	–	1,295.8	–	–	1.7
Trade receivables	17.8	–	–	70.5	1.5	16.2	–	9.6	34.4	1.5
Interest receivable	–	24.1	–	0.5	–	–	15.9	–	–	–
Derivative financial assets	0.3	9.9	–	–	–	–	35.7	–	–	–
Loans payable	(107.1)	(3,661.4)	–	–	–	–	(2,302.8)	–	–	–
Trade payables	(0.4)	(0.1)	(4.8)	(179.0)	(11.9)	(35.4)	(0.1)	(4.8)	(179.7)	–
Capital payables	–	–	–	(11.2)	–	–	–	–	–	–
Interest payable	(0.1)	(25.9)	–	–	–	–	(32.9)	–	–	–
Derivative financial liabilities	(6.7)	(27.1)	–	–	–	–	(33.9)	–	–	–

- (i) The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received in relation to intra-group transactions.
- (ii) On 1 January 2012, as part of an Iberdrola group reorganisation, the group acquired certain renewable energy companies from another Iberdrola group company. On 1 July 2011, a group restructuring exercise took place to align the operational structure of ScottishPower with the operational structure of Iberdrola. Details of the transactions that the company participated in, in both years, are set out in Note 34.

(b) Remuneration of key management personnel

The remuneration of the key management personnel of the SPUK group is set out below. As all of the key management personnel are remunerated for their work for the Iberdrola group, it has not been possible to apportion the remuneration specifically in respect of services to the SPUK group. Eight of the key management personnel were paid by companies within the SPUK group.

	2012 £m	2011 £m
Short-term employee benefits	4.8	3.7
Post-employment benefits	0.4	0.4
Other long-term benefits	0.3	0.3
Termination benefits	–	1.0
Share-based payments	1.2	1.7
	6.7	7.1

(c) Directors' remuneration

The total emoluments of the directors that provided qualifying services to the SPUK group are shown below. As these directors are remunerated for their work for the Iberdrola group as a whole, it has not been possible to apportion the remuneration specifically in respect of services to the SPUK group. During the year, all but one of the directors were paid by the company.

	2012 £000	2011 £000
Executive directors		
Salary	492	482
Bonus	241	345
Benefits in kind	44	115
Pension costs	14	24
Total	791	966

- (i) Two directors (2011 two) had retirement benefits accruing under defined benefit pension schemes. During the year two directors (2011 one) had retirement benefits accruing under a defined contribution pension scheme.
- (ii) During the year, two directors (2011 two) received shares under a long-term share incentive scheme.
- (iii) During the year three directors (2011 three) exercised share options.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

32 RELATED PARTY TRANSACTIONS *continued*

	2012 £000	2011 £000
Highest paid director		
Salary	165	220
Bonus	103	175
Benefits in kind	6	98
Pension costs	–	24
Total	274	517

(iv) At the end of the year, the highest paid director had an accrued pension benefit of £35,986 (2011 £nil).

(v) The highest paid director received shares under a long-term incentive scheme during both years.

(vi) The highest paid director exercised share options during both years.

(d) Ultimate parent company

The directors regard Iberdrola S.A. as the ultimate parent company, which is also the parent company of the largest group in which the results of the company are consolidated. Copies of the consolidated Accounts of Iberdrola S.A. may be obtained from Iberdrola S.A., Torre Iberdrola, Plaza Euskadi 5, 48009, Bilbao, Spain. The parent company of the smallest group in which the results of the company are consolidated is Scottish Power UK Holdings Limited. Copies of the consolidated Accounts of Scottish Power UK Holdings Limited may be obtained from The Secretary, Scottish Power UK Holdings Limited, 1 Atlantic Quay, Glasgow, G2 8SP.

33 AUDITORS' REMUNERATION

	2012 £m	2011 £m
Audit of the company's annual group accounts	0.2	0.2
Audit of the company's subsidiaries pursuant to legislation	0.9	0.9
Audit fees	1.1	1.1
Other services pursuant to legislation	0.1	0.1
Other services	0.4	0.1
Non-audit fees	0.5	0.2
Total	1.6	1.3

For the year ended 31 December 2012, all fees paid to the auditors of £1.6 million (2011 £1.3 million) were charged to Profit from operations.

34 BUSINESS COMBINATIONS

(a) Group restructuring

As part of an Iberdrola group restructuring exercise to align the operational structure of ScottishPower with the operational structure of the Iberdrola group, the following transactions have taken place during the current and prior years;

(i) Two new holding companies were incorporated within the Scottish Power UK plc group namely, Scottish Power Energy Networks Holdings Limited ("SPENH") and Scottish Power Generation Holdings Limited ("SPGH"). Both companies are direct subsidiaries of the company and are funded by a combination of debt and equity.

(ii) On 1 July 2011, those entities within the group deemed to be part of the Energy Networks business were transferred to SPENH and those entities within the group deemed to be part of the Energy Retail and Energy Wholesale businesses were transferred to SPGH. These transfers were undertaken at the book value of the investment and had no impact on the net profit or net assets of the group.

(iii) Similarly on the same date, certain entities deemed to be part of the Energy Wholesale business (namely ScottishPower Energy Management Limited, ScottishPower Energy Management (Agency) Limited, ScottishPower (DCL) Limited and its subsidiaries, SP Gas Transportation Cockenzie Limited and SP Gas Transportation Hatfield Limited were transferred from SPUKH for a cash consideration of £65.3 million. These transactions are deemed to be business combinations under common control and have been accounted for under the pooling of interests method in the consolidated Accounts as described in Note 2. The impact of these transactions on the net assets of the group is set out in Note (b).

(iv) On 1 January 2012, ScottishPower Renewable Energy Limited ("SPREL"), the holding company of the group conducting Iberdrola's renewable energy activity in the UK was transferred to the group from Iberdrola Finance UK Limited ("IBF"), a subsidiary of Iberdrola S.A., for a cash consideration of £27.8 million. This transaction is deemed to be a business combination under common control and has been accounted for under the pooling of interests method in the consolidated Accounts as described in Note 2. The impact of the transfer of these companies on the net assets of the group is set out in Note (c).

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

34 BUSINESS COMBINATIONS *continued*

(b) Book values of assets and liabilities at 1 July 2011

The details of the book value of the assets and liabilities acquired by the group as part of the restructuring are shown below:

	Notes to the accounts	ScottishPower Energy Management Limited £m	ScottishPower Energy Management (Agency) Limited £m	ScottishPower (DCL) Limited (Note (iii)) £m	Total £m
Book values of assets and liabilities at 1 July 2011					
Intangible assets	7	5.2	–	13.3	18.5
Property, plant and equipment	8	15.8	–	271.8	287.6
Derivative financial assets		379.3	–	96.9	476.2
Deferred tax	22	11.7	–	(37.6)	(25.9)
Inventories		191.8	–	–	191.8
Trade and other receivables		695.6	–	43.6	739.2
Receivables due from Iberdrola group companies - loans		–	–	0.2	0.2
Cash		0.1	5.4	–	5.5
Deferred income	15	–	–	(6.1)	(6.1)
Derivative financial liabilities		(397.7)	–	(60.4)	(458.1)
Provisions	17	(41.7)	–	(9.1)	(50.8)
Trade and other payables		(301.4)	–	(65.1)	(366.5)
Payables due to Iberdrola group companies - loans		(417.2)	–	(156.8)	(574.0)
Current tax		(25.5)	(0.8)	(36.1)	(62.4)
Net assets		116.0	4.6	54.6	175.2
Cash consideration (Note (iv))		50.0	4.0	11.3	65.3
Pooling of interest recognised in equity	13	66.0	0.6	43.3	109.9
Total		116.0	4.6	54.6	175.2

(i) The above companies were acquired by SPGH from SPUKH for a cash consideration of £65.3 million.

(ii) In addition, SPGH acquired the entire share capital of SP Gas Transportation Hatfield Limited and SP Gas Transportation Cockenzie Limited from SPUKH for a consideration of £2 each being the net asset values of those companies.

(iii) The net assets shown in respect of this company are the consolidated net assets for ScottishPower (DCL) Limited and its subsidiaries.

(iv) The analysis of cash flow in respect of the above acquisitions is detailed below:

	£m
Cash consideration	(65.3)
Net cash and cash equivalents acquired	(568.3)
Cash outflows on group restructuring (included in cash flows from investing activities)	(633.6)

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

34 BUSINESS COMBINATIONS *continued*

(c) Book values of assets and liabilities at 1 January 2012

The details of the book value of the assets and liabilities acquired by the group as part of the restructuring are shown below:

	Notes to the Accounts	ScottishPower Renewable Energy Limited (Note (ii)) £m
Book values of assets and liabilities at 1 January 2012		
Intangible assets	7	893.4
Property, plant and equipment	8	1,836.9
Investments		0.6
Derivative financial assets		0.4
Trade and other receivables		23.0
Receivables due from Iberdrola group companies – loans		76.1
Current tax		26.6
Cash		4.5
Deferred income	15	(2.2)
Derivative financial liabilities		(33.1)
Provisions	17	(41.5)
Deferred tax	22	(397.2)
Trade and other payables		(36.6)
Current payables due to Iberdrola group companies – loans		(912.8)
Non-current payables due to Iberdrola group companies – loans		(76.3)
Net assets		1,361.8
Cash consideration (Note (iii))		27.8
Pooling of interest recognised in equity	13	1,333.7
Non-controlling interests	14	0.3
Total		1,361.8

(i) SPREL was acquired by SPUK from IBF for a cash consideration of £27.8 million.

(ii) The net assets shown in respect of this company are the consolidated net assets for SPREL and its subsidiaries, as included in the Iberdrola S.A. Consolidated Financial Statements and include the fair value attributed to the renewables segment when purchased by Iberdrola in 2007.

(iii) The analysis of cash flow in respect of the above acquisitions is detailed below:

	£m
Cash consideration	(27.8)
Net cash and cash equivalents acquired	(832.2)
Cash outflows on group restructuring (included in cash flows from investing activities)	(860.0)

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

35 ACCOUNTING DEVELOPMENTS

In preparing these Accounts, the group has applied all relevant IAS, IFRS and IFRIC Interpretations which have been adopted by the EU as of the date of approval of these Accounts and which are mandatory for the financial year ended 31 December 2012.

For the year ended 31 December 2012, the group has applied the following amendment for the first time:

- Amendments to IFRS 7 'Financial Instruments: Disclosures – Transfers of Financial Assets'

The application of this amendment did not have a significant effect on the the group results or financial policy.

The following new standards and amendments have effective dates after the date of these financial statements and have not yet been implemented by the group:

Standard	Notes	IASB Effective Date (for periods commencing on or after)	Planned date of application by the group
• Amendments to IAS 1 'Presentation of Items of Other Comprehensive Income'	(a)	1 July 2012	1 January 2013
• IAS 19 (Revised) 'Employee Benefits'	(b)	1 January 2013	1 January 2013
• IFRS 9 'Financial Instruments' and subsequent amendments	(c), (d)	1 January 2015	1 January 2015
• Amendments to IAS 12 'Income Taxes: Deferred tax - Recovery of Underlying Assets'	(a), (e)	1 January 2012	1 January 2013
• IFRS 10 'Consolidated Financial Statements'	(d), (f)	1 January 2013	1 January 2014
• IFRS 11 'Joint Arrangements'	(d), (f)	1 January 2013	1 January 2014
• IFRS 12 'Disclosure of Interests in Other Entities'	(d), (f)	1 January 2013	1 January 2014
• IFRS 13 'Fair Value Measurement'	(g)	1 January 2013	1 January 2013
• IAS 27 (Revised) 'Separate Financial Statements'	(d), (f)	1 January 2013	1 January 2014
• IAS 28 (Revised) 'Investments in Associates and Joint Ventures'	(d), (f)	1 January 2013	1 January 2014
• Amendments to IFRS 7 'Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities'	(a)	1 January 2013	1 January 2013
• Amendments to IAS 32 'Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities'	(a)	1 January 2014	1 January 2014
• Amendments to IFRS 10, IFRS 11 and IFRS 12 'Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance'	(d), (f)	1 January 2013	1 January 2014
• Amendments to IFRS 10, IFRS 12 and IAS 27 'Investment Entities'	(c), (d)	1 January 2014	1 January 2014
• Annual Improvements to IFRSs (2009-2011)	(a)	1 January 2013	1 January 2013
• IFRIC 21 'Leases'	(c), (d)	1 January 2014	1 January 2014
• Amendments to IAS 36 'Impairment of Asset – Recoverable Amount Disclosures for Non-Financial Assets'	(c), (d)	1 January 2014	1 January 2014

- (a) The group considers that the future application of this standard/amendment will not have a significant effect on the results or financial policy.
- (b) The revisions to IAS 19 are expected to have a significant impact on the results of the group from 1 January 2013. The discount rate (determined by market yields of similar high quality corporate bonds) will be applied to both the scheme liabilities and the scheme assets (previously expected return on assets). The estimated impact of this change is a £40.0 million reduction to finance income. There is no impact on reserves. Additional disclosure will also be required to present more detailed sensitivity analysis and a profile of the cash flow impact of the liability.
- (c) These pronouncements have not yet been adopted by the EU.
- (d) The group is currently considering the impact of these pronouncements.
- (e) The IASB effective date of this amendment was for periods commencing on or after 1 January 2012. However the amendment was not effective in the EU until 1 January 2013.
- (f) The IASB effective date of these pronouncements is for periods commencing on or after 1 January 2013. However the EU permits adoption of these pronouncements for periods commencing on or after no later than 1 January 2014.
- (g) The application of IFRS 13 for the first time as from 1 January 2013 is not expected to have a significant impact on the group's results or financial policy as the measurement framework is not significantly different to the group's current practice. Additional disclosures regarding assets and liabilities measured at fair value and the sensitivity around the fair values will be required.
- (h) The group has chosen not to early adopt any of these standards/amendments for year ended 31 December 2012.

36 GOING CONCERN

The group's business activities together with the factors likely to affect its future development and position are set out in the Directors' Report on pages 1 to 15.

The group has recorded a profit after tax in both the current and previous financial years and the group's balance sheet shows that it has net current liabilities of £1,928.7 million and net assets of £3,778.5 million at its most recent balance sheet date.

The group is ultimately owned by Iberdrola S.A. and it participates in the Iberdrola group's centralised treasury arrangements and so shares banking facilities with its parent companies and fellow subsidiaries. As a consequence, the group depends, in part, on the ability of the Iberdrola group to continue as a going concern. The directors have considered the group's funding relationship with Iberdrola to date and have considered available relevant information relating to Iberdrola's ability to continue as a going concern. In addition, the directors have no reason to believe that the Iberdrola group will not continue to fund the group to enable it to continue in operational existence.

On the basis of these considerations, the directors have a reasonable expectation that the group will be able to continue in operational existence for the foreseeable future. Therefore, they continue to adopt the going concern basis of accounting in preparing the Accounts.

NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2012

Subsidiaries	Class of share capital	Proportion of shares held	Activity
Energy Networks			
Manweb Services Limited	Ordinary shares £1	100%	Operation of private electricity distribution network
Scottish Power Energy Networks Holdings Limited	Ordinary shares £1	100% (b)	Holding company
SP Distribution Limited	Ordinary shares £1	100%	Ownership and operation of distribution network within the Scottish Power area
SP Manweb plc	Ordinary shares 50p	100%	Ownership and operation of distribution network within the Mersey and North Wales area
SP Network Connections Limited	Ordinary shares £1	100%	Multi-utility design and construction service
SP Power Systems Limited	Ordinary shares £1	100%	Provision of asset management services and multi-utility design and construction service
SP Transmission Limited	Ordinary shares £1	100%	Ownership and operation of transmission network within the Scottish Power area
SPD Finance UK plc	Ordinary shares £1	100%	Finance company
Energy Wholesale			
Scottish Power Generation Holdings Limited	Ordinary shares £1	100% (b)	Holding company
ScottishPower (DCL) Limited	Ordinary shares £1	100%	Electricity generation
ScottishPower (DCOL) Limited	Ordinary shares £1	100%	Management services
ScottishPower Energy Management Limited	Ordinary shares £1	100%	Wholesale energy management company engaged in purchase and sale of electricity, gas and coal
ScottishPower Energy Management (Agency) Limited	Ordinary shares £1	100%	Agent for energy management activity of ScottishPower Energy Management Limited and Scottish Power UK plc
ScottishPower Generation Limited	Ordinary shares £1	100%	Electricity generation
ScottishPower (SCPL) Limited	'A' and 'B' Ordinary shares £1	100%	Electricity generation
ScottishPower (SOCL) Limited	'A' and 'B' Ordinary shares £1	100%	Management services
SMW Limited	Ordinary shares £1	100%	Wastewater treatment
SP Gas Transportation Cockenzie Limited	Ordinary shares £1	100%	Holder of Gas Transporter Licence
SP Gas Transportation Hatfield Limited	Ordinary shares £1	100%	Holder of Gas Transporter Licence
Energy Retail			
ScottishPower Energy Retail Limited	Ordinary shares £1	100%	Supply of electricity and gas to domestic and business customers
SP Dataserve Limited	Ordinary shares £1	100%	Data collection, data aggregation, meter operation and revenue protection
Renewables			
ScottishPower Renewable Energy Limited	Ordinary shares £1	100%(a), (b)	Holding company
ScottishPower Renewables (UK) Limited (Northern Ireland)	Ordinary shares £1	100%	Construction and operation of wind powered electricity generation
ScottishPower Renewables (WODS) Limited	Ordinary shares £1	100%	Development, construction and operation of offshore windfarm
Coldham Windfarm Limited	Ordinary shares £1	80%	Electricity generation
Other			
ScottishPower Insurance Limited (Isle of Man)	Ordinary shares £1	100%	Insurance
ScottishPower Investments Limited	Ordinary shares £1	100% (b)	Holding company
Equity investments			
Jointly controlled entities			
ScotAsh Limited	'B' Ordinary shares £1	100% (c)	Sales of ash and ash-related cementitious products
NGET/SPT Upgrades Limited	'B' ordinary shares £1	100% (c)	Development of offshore HVDC West Coast transmission link
Celtpower Limited	Ordinary shares £1	50%	Electricity generation
East Anglia Offshore Wind Limited	Ordinary shares £1	50%	Offshore wind farm development

Notes

- (a) This company and its subsidiaries were acquired from Iberdrola Finance (UK) Limited on 1 January 2012 (see Note 34).
- (b) The investment in this company is a direct holding of Scottish Power UK plc at 31 December 2012.
- (c) Represents 50% of the total issued share capital.
- (d) The company considers that to give full particulars of all entities would lead to a statement of excessive length. The information above includes the entities whose results or financial position, in the opinion of the company, principally affect the results or financial position of the group.
- (e) All companies are incorporated in Great Britain, unless otherwise stated.

SCOTTISH POWER UK PLC
COMPANY BALANCE SHEETS
at 31 December 2012 and 31 December 2011

	Notes	2012 £m	2011 £m
ASSETS			
NON-CURRENT ASSETS			
Intangible assets		27.9	39.1
Other intangible assets	37	27.9	39.1
Property, plant and equipment		24.5	23.7
Property, plant and equipment in use	38	20.8	23.4
Property, plant and equipment in course of construction	38	3.7	0.3
Trade and other receivables	39	1,285.0	390.0
Financial assets		1,133.0	1,122.8
Investments in subsidiaries	40	1,099.3	1,071.5
Other investments	40	1.0	1.0
Derivative financial instruments	42, 49	32.7	50.3
Deferred tax asset	41	68.3	21.6
NON-CURRENT ASSETS		2,538.7	1,597.2
CURRENT ASSETS			
Trade and other receivables	39	1,565.7	1,327.5
Current tax receivables		7.5	18.8
Financial assets		1.4	1.6
Derivative financial instruments	42, 49	0.7	0.7
Cash and cash equivalents and term deposits	42	0.7	0.9
CURRENT ASSETS		1,574.6	1,347.9
TOTAL ASSETS		4,113.3	2,945.1
EQUITY AND LIABILITIES			
EQUITY			
Of shareholders of the parent		2,356.2	1,432.2
Share capital	43, 44	872.0	872.0
Share premium	44	398.2	398.2
Hedge reserve	44	–	0.1
Other reserves	44	8.2	8.2
Retained earnings	44	1,077.8	153.7
TOTAL EQUITY		2,356.2	1,432.2
NON-CURRENT LIABILITIES			
Deferred income	45	–	2.7
Provisions		274.6	65.5
Provision for retirement benefit obligations	46	259.9	49.6
Other provisions	47	14.7	15.9
Bank borrowings and other financial liabilities		1,229.9	1,238.1
Loans and other borrowings	48	1,229.9	1,238.1
Trade and other payables	50	1.8	1.7
NON-CURRENT LIABILITIES		1,506.3	1,308.0
CURRENT LIABILITIES			
Provisions	47	4.6	6.6
Bank borrowings and other financial liabilities		167.7	86.6
Loans and other borrowings	48	167.6	86.6
Derivative financial liabilities	42, 49	0.1	–
Trade and other payables	50	78.5	111.7
CURRENT LIABILITIES		250.8	204.9
TOTAL LIABILITIES		1,757.1	1,512.9
TOTAL EQUITY AND LIABILITIES		4,113.3	2,945.1

Approved by the board on 25 June 2013 and signed on its behalf by:



Daniel Alcain Lopez
Director

Notes 1 to 5 and the accompanying Notes 37 to 54 are an integral part of the company balance sheets as at 31 December 2012 and 31 December 2011.

SCOTTISH POWER UK PLC

COMPANY STATEMENTS OF COMPREHENSIVE INCOME

for the years ended 31 December 2012 and 31 December 2011

	2012 £m	2011 £m
NET PROFIT FOR THE YEAR	1,114.4	185.1
OTHER COMPREHENSIVE INCOME		
Cash flow hedges:		
Change in the value of cash flow hedges	(0.1)	0.4
Tax on items relating to cash flow hedges	–	(0.1)
	(0.1)	0.3
Actuarial losses on retirement benefits:		
Actuarial losses on retirement benefits	(243.9)	(54.6)
Tax relating to actuarial losses on retirement benefits	53.6	12.3
	(190.3)	(42.3)
OTHER COMPREHENSIVE INCOME FOR THE YEAR	(190.4)	(42.0)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	924.0	143.1

Total comprehensive income for both years is wholly attributable to the equity holders of Scottish Power UK plc.

COMPANY STATEMENTS OF CHANGES IN EQUITY

for the years ended 31 December 2012 and 31 December 2011

	Ordinary share capital £m	Share premium £m	Hedge reserve £m	Other reserves £m	Retained earnings £m	Total equity £m
At 1 January 2011	872.0	398.2	(0.2)	8.2	210.9	1,489.1
Total comprehensive income for the year	–	–	0.3	–	142.8	143.1
Dividends	–	–	–	–	(200.0)	(200.0)
At 1 January 2012	872.0	398.2	0.1	8.2	153.7	1,432.2
Total comprehensive income for the year	–	–	(0.1)	–	924.1	924.0
At 31 December 2012	872.0	398.2	–	8.2	1,077.8	2,356.2

Notes 1 to 5 and the accompanying Notes 37 to 54 are an integral part of the company statements of comprehensive income and the company statements of changes in equity for the years ended 31 December 2012 and 31 December 2011.

SCOTTISH POWER UK PLC
COMPANY CASH FLOW STATEMENTS
for the years ended 31 December 2012 and 31 December 2011

	2012 £m	2011 £m
Cash flows from operating activities		
Profit before tax	1,103.1	183.8
Adjustments for:		
Depreciation and amortisation	32.4	36.2
Change in provisions	(2.4)	0.5
Finance income and costs	13.8	7.9
Shareholding income	(1,122.0)	(190.0)
Loss on disposal/write-off of non-current assets	0.2	2.6
Movement in retirement benefits	(4.1)	(13.9)
Movement in deferred income	(2.7)	2.7
Changes in working capital:		
Change in trade and other receivables	2.0	19.6
Change in trade and other payables	(38.5)	21.0
Provisions paid	(2.9)	(2.9)
Income taxes received	29.5	230.0
Interest received	31.1	83.8
Dividends received	1,122.0	190.4
Net cash flows from operating activities (i)	1,161.5	571.7
Cash flows from investing activities		
Acquisition of subsidiaries	(27.8)	(953.8)
Investments in intangible assets	(11.4)	(8.1)
Investments in property, plant and equipment	(4.6)	(3.6)
Proceeds from disposal of available-for-sale investments	–	9.4
Proceeds from disposal of property, plant and equipment	1.0	0.2
Proceeds from disposal of subsidiaries	–	660.5
Net cash flows from investing activities (ii)	(42.8)	(295.4)
Cash flows from financing activities		
(Increase)/decrease in amounts due from Iberdrola group companies	(890.0)	350.0
Dividends paid to company's equity holders	–	(200.0)
Cash inflows from borrowings	0.4	17.8
Interest paid	(71.9)	(87.7)
Repayments of borrowings	(9.2)	(237.8)
Net cash flows from financing activities (iii)	(970.7)	(157.7)
Net increase in cash and cash equivalents (i)+(ii)+(iii)	148.0	118.6
Cash and cash equivalents at beginning of year	1,205.4	1,086.8
Cash and cash equivalents at end of year	1,353.4	1,205.4
Cash and cash equivalents at end of year comprises:		
Company balance sheet cash and cash equivalents and term deposits	0.7	0.9
Receivables due from Iberdrola group companies – loans	1,483.5	1,245.3
Payables due to Iberdrola group companies – loans	(130.8)	(40.8)
Company cash flow statement cash and cash equivalents	1,353.4	1,205.4

Notes 1 to 5 and the accompanying Notes 37 to 54 are an integral part of the company cash flow statements for the year ended 31 December 2012 and 31 December 2011.

NOTES TO THE COMPANY ACCOUNTS

31 December 2012

37 INTANGIBLE ASSETS

	Computer software £m
Year ended 31 December 2011	
Cost:	
At 1 January 2011	309.7
Additions	8.1
Disposals	(9.0)
At 31 December 2011	308.8
Amortisation:	
At 1 January 2011	252.9
Amortisation for the year	23.3
Disposals	(6.5)
At 31 December 2011	269.7
Net book value:	
At 31 December 2011	39.1
At 1 January 2011	56.8

	Computer software £m
Year ended 31 December 2012	
Cost:	
At 1 January 2012	308.8
Additions	11.4
At 31 December 2012	320.2
Amortisation:	
At 1 January 2012	269.7
Amortisation for the year	22.6
At 31 December 2012	292.3
Net book value:	
At 31 December 2012	27.9
At 1 January 2012	39.1

(a) The cost of fully amortised computer software still in use at 31 December 2012 was £264.3 million (2011 £220.6 million)

38 PROPERTY, PLANT AND EQUIPMENT

	Property, plant and equipment in use £m	Property, plant and equipment in progress £m	Total £m
Year ended 31 December 2011			
Cost:			
At 1 January 2011	116.3	–	116.3
Additions	3.7	0.3	4.0
Disposals	(4.7)	–	(4.7)
At 31 December 2011	115.3	0.3	115.6
Depreciation:			
At 1 January 2011	83.4	–	83.4
Charge for the year	12.9	–	12.9
Disposals	(4.4)	–	(4.4)
At 31 December 2011	91.9	–	91.9
Net book value:			
At 31 December 2011	23.4	0.3	23.7
At 1 January 2011	32.9	–	32.9

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

38 PROPERTY, PLANT AND EQUIPMENT *continued*

	Property, plant and equipment in use £m	Property, plant and equipment in progress £m	Total £m
Year ended 31 December 2012			
Cost:			
At 1 January 2012	115.3	0.3	115.6
Additions	8.4	3.4	11.8
Disposals	(5.4)	–	(5.4)
At 31 December 2012	118.3	3.7	122.0
Depreciation:			
At 1 January 2012	91.9	–	91.9
Charge for the year	9.8	–	9.8
Disposals	(4.2)	–	(4.2)
At 31 December 2012	97.5	–	97.5
Net book value:			
At 31 December 2012	20.8	3.7	24.5
At 1 January 2012	23.4	0.3	23.7

(a) The cost of fully depreciated property, plant and equipment still in use at 31 December 2012 was £74.0 million (2011 £55.3 million).

(b) Included in the cost of property, plant and equipment at 31 December 2012 are assets in use not subject to depreciation, being land, of £nil (2011 £0.1 million).

39 TRADE AND OTHER RECEIVABLES

	Notes	2012 £m	2011 £m
Current receivables:			
Receivables due from Iberdrola group companies – trade		35.3	32.6
Receivables due from Iberdrola group companies – loans	(a)	1,483.5	1,245.3
Receivables due from Iberdrola group companies – interest		32.2	25.2
Trade receivables		3.3	2.1
Prepayments		11.4	17.8
Other tax receivables		–	4.5
		1,565.7	1,327.5
Non-current receivables:			
Receivables due from Iberdrola group companies – loans	(b)	1,280.0	390.0
Prepayments		5.0	–
		1,285.0	390.0

(a) Interest on current loans due from Iberdrola group companies is payable at 1% above the Bank of England base rate and the loans are repayable on demand.

(b) Non-current loans due from Iberdrola group companies comprises £960.0 million (2011 £nil) of loans due to be repaid in 2022 which earn interest annually at 3.416% and £320.0 million (2011 £390.0 million) of loans due to be repaid in 2029 which earn interest annually at 3.365% above 12 month LIBOR.

(c) At 31 December 2012 trade receivables of £15.1 million (2011 £30.5 million), were past due but not impaired:

	2012 £m	2011 £m
Past due but not impaired:		
Less than 3 months	10.7	27.7
Between 3 and 6 months	4.4	1.0
Between 6 and 12 months	–	1.8
	15.1	30.5

40 INVESTMENTS

	Notes	Subsidiary undertakings shares £m	Other investments (Note (a)) £m	Total £m
At 1 January 2011		778.2	1.2	779.4
Additions	(b)	953.8	–	953.8
Disposals	(b)	(660.5)	(0.2)	(660.7)
At 1 January 2012		1,071.5	1.0	1,072.5
Additions	(c)	27.8	–	27.8
At 31 December 2012		1,099.3	1.0	1,100.3

(a) At 31 December 2012 the company held £1.0 million (2011 £1.0 million) of investments for which no quoted market price is available and whose fair value could not be reliably measured.

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

40 OTHER INVESTMENTS *continued*

- (b) As part of a group restructuring during 2011 to align the operational structure of ScottishPower with the operational structure of the Iberdrola group, the following transactions took place:
- (i) Two new intermediate holding companies were formed: Scottish Power Generation Holdings Limited ("SPGH") and Scottish Power Energy Networks Holdings Limited ("SPENH"). The company's total investment in the share capital of these companies is £953.8 million.
- (ii) On 1 July 2011, the company transferred ownership of its investments in ScottishPower Generation Limited and SP Dataserve Limited to SPGH, for a total consideration of £148.3 million, being the carrying value of those investments.
- (iii) On July 2011, the company also transferred its 50% holding in SP Network Connections Limited to its subsidiary, SP Power Systems Limited ("SPPS") for a consideration of £1.0 million, being the carrying value of that investment. The company then transferred ownership of its investments in SPPS and SP Transmission Limited to SPENH, for a total consideration of £511.2 million, being the carrying value of those investments.
- (c) On 1 January 2012, ScottishPower Renewable Energy Limited, the holding company of the group conducting Iberdrola's renewable energy activity in the UK was transferred from Iberdrola Finance UK Limited ("IBF"), a subsidiary of Iberdrola S.A. to the company for a cash consideration of £27.8 million. This transaction is described in detail at Note 34.
- (d) The principal subsidiaries and jointly controlled entities are listed on page 60.

41 DEFERRED TAX ASSET

Deferred tax recognised in the Accounts is as follows:

	Accelerated capital allowances £m	Derivative financial instruments £m	Retirement benefits £m	Other temporary differences £m	Total £m
At 1 January 2011	2.4	2.0	6.8	8.8	20.0
Credit/(charge) to income statement	3.1	(0.3)	(6.7)	(6.7)	(10.6)
Recorded in the statement of comprehensive income	–	(0.1)	12.3	–	12.2
At 1 January 2012	5.5	1.6	12.4	2.1	21.6
Credit/(charge) to income statement	1.1	(0.5)	(6.2)	(1.3)	(6.9)
Recorded in the statement of comprehensive income	–	–	53.6	–	53.6
At 31 December 2012	6.6	1.1	59.8	0.8	68.3

- (a) At 31 December 2012, the company had unutilised capital losses of £3.1 million (2011 £3.9 million). No deferred tax asset has been recognised in the accounts due to the unpredictability of suitable future profit streams against which these losses may be utilised.
- (b) The government has announced that it intends to reduce the rate of UK corporation tax to 20% by 1 April 2015. The rate of corporation tax reduced from 28% to 26% on 1 April 2011 and to 24% on 1 April 2012. A further reduction to 23%, effective from 1 April 2013, was enacted at the balance sheet date. These changes have reduced the tax rate expected to apply when temporary differences reverse. Reductions of another 3% are expected and will reduce the property, plant and equipment element of the deferred tax provision. The estimated impact of these changes will be a reduction of £0.9 million. It is not possible to quantify the impact of the rate reductions on other elements of the deferred tax balance.

42 MEASUREMENT OF FINANCIAL INSTRUMENTS

The table below sets out the carrying amount and fair value of the company's financial instruments:

		2012		2011	
		Carrying Amount £m	Fair Value £m	Carrying Amount £m	Fair Value £m
	Notes				
Financial assets					
Derivative financial instruments	(a)	33.4	33.4	51.0	51.0
Current receivables	(b)	1,554.3	1,554.3	1,305.2	1,305.2
Non-current receivables	(c)	1,280.0	1,565.2	390.0	390.0
Other investments		1.0	1.0	1.0	1.0
Short term deposits	(d)	0.7	0.7	0.9	0.9
Financial liabilities					
Derivative financial instruments	(a)	(0.1)	(0.1)	–	–
Loans and other borrowings	(e)	(1,397.5)	(2,406.2)	(1,324.7)	(1,611.2)
Payables	(b)	(76.5)	(76.5)	(111.0)	(111.0)

The carrying amount of these financial instruments is calculated as set out in Note 3G. With the exception of non-current receivables and loans and borrowings, the carrying value of financial instruments is a reasonable approximation of fair value. The fair value of loans and borrowings is calculated as set out in Note (d).

- (a) Further detail on derivative financial instruments is disclosed in Note 49.
- (b) Balances outwith the scope of IFRS 7 have been excluded principally prepayments, tax receivables and tax payables.
- (c) The fair value of non-current receivables is calculated using the most recently traded price to the year end date, where applicable, or alternatively a discounted cash flow.
- (d) Cash is comprised of deposits with banks and other short-term deposits. As a general rule, cash deposited with banks earns interest at rates similar to market rates on daily deposits.
- (e) The fair value of listed debt is calculated using the most recently traded price to the year-end date and the fair value of all other loans and borrowings is calculated using a discounted cash flow.

The company holds certain financial instruments which are measured in the balance sheet at fair value. The company uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

All derivatives held by the company are Level 2.

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

43 SHARE CAPITAL

	2012 £m	2011 £m
Authorised:		
3,000,000,002 (2011 3,000,000,002) ordinary shares of 50p each	1,500.0	1,500.0
Allotted, called up and fully paid:		
1,743,983,102 (2011 1,743,983,102) ordinary shares of 50p each	872.0	872.0

44 ANALYSIS OF MOVEMENTS IN EQUITY ATTRIBUTABLE TO THE EQUITY HOLDERS OF SCOTTISH POWER UK PLC

	Share capital £m	Share premium (Note(a)) £m	Hedge reserve (Note(b)) £m	Other reserves (Note(c)) £m	Retained earnings (Note(d)) £m	Total £m
At 1 January 2011	872.0	398.2	(0.2)	8.2	210.9	1,489.1
Profit for the year attributable to the equity holders of Scottish Power UK plc	–	–	–	–	185.1	185.1
Changes in the value of cash flow hedges	–	–	0.4	–	–	0.4
Actuarial losses on retirement benefits	–	–	–	–	(54.6)	(54.6)
Tax on items relating to cash flow hedges	–	–	(0.1)	–	–	(0.1)
Tax on items relating to actuarial losses on retirement benefits	–	–	–	–	12.3	12.3
Dividends	–	–	–	–	(200.0)	(200.0)
At 1 January 2012	872.0	398.2	0.1	8.2	153.7	1,432.2
Profit for the year attributable to the equity holders of Scottish Power UK plc	–	–	–	–	1,114.4	1,114.4
Changes in the value of cash flow hedges	–	–	(0.1)	–	–	(0.1)
Actuarial losses on retirement benefits	–	–	–	–	(243.9)	(243.9)
Tax on items relating to actuarial losses on retirement benefits	–	–	–	–	53.6	53.6
At 31 December 2012	872.0	398.2	–	8.2	1,077.8	2,356.2

(a) The share premium account represents consideration received for shares issued in excess of their nominal amount.

(b) The hedge reserve represents the balance of gains and losses on cash flow hedges (net of taxation) not yet transferred to income or the carrying amount of a non-financial asset.

(c) Other reserves at 31 December 2012 comprises a capital redemption reserve of £8.2 million (2011 £8.2 million). The capital redemption reserve comprises the nominal value of the company's ordinary share capital purchased by the company in previous years.

(d) Retained earnings comprise the cumulative balance of profit and losses recognised in the financial statements as adjusted for transactions with shareholders, principally dividends.

(e) The changes in the hedge reserve arising from valuation adjustments to hedging derivatives are set out below:

	Interest rate swaps £m	Foreign exchange rate hedges £m	Tax effect £m	Total £m
Cash flow hedges				
At 1 January 2011	(0.3)	–	0.1	(0.2)
Removed from equity and recognised in carrying amount of hedged items	–	0.1	–	0.1
Removed from equity and recognised in income statement	0.3	–	(0.1)	0.2
At 1 January 2012	–	0.1	–	0.1
Effective cash flow hedges recognised	–	(0.1)	–	(0.1)
At 31st December 2012	–	–	–	–

(i) All amounts included in the hedge reserve mature within one year.

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

45 DEFERRED INCOME

	At 1 January 2011 £m	Receivable during year £m	At 31 December 2011 £m
Year ended 31 December 2011			
Other revenue-related deferred income	–	2.7	2.7
Total deferred income	–	2.7	2.7

	At 1 January 2012 £m	Released to income statement £m	At 31 December 2012 £m
Year ended 31 December 2012			
Other revenue-related deferred income	2.7	(2.7)	–
Total deferred income	2.7	(2.7)	–

46 RETIREMENT BENEFIT OBLIGATIONS

The amounts recognised in the balance sheet in respect of retirement benefit obligations are detailed below:

	2012			2011		
	SPPS £m	UURBS £m	Total £m	SPPS £m	UURBS £m	Total £m
Non-current liabilities	253.8	6.1	259.9	44.5	5.1	49.6

The company recognises the pension scheme deficit in the balance sheet for the schemes for which it is the sponsoring employer as there is no appropriate contractual agreement or group policy to allocate the deficit on a legal entity basis. Detailed disclosures are provided in Note 16 of the group financial statements.

47 OTHER PROVISIONS

	Notes	At 1 January 2011 £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	Released during year £m	At 31 December 2011 £m
Year ended 31 December 2011							
Reorganisation and restructuring	(a)	1.9	1.3	–	(0.8)	(0.8)	1.6
Onerous contracts	(b)	22.3	–	0.7	(2.1)	–	20.9
		24.2	1.3	0.7	(2.9)	(0.8)	22.5

	Notes	At 1 January 2012 £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	Released during year £m	At 31 December 2012 £m
Year ended 31 December 2012							
Reorganisation and restructuring	(a)	1.6	–	–	–	(1.6)	–
Onerous contracts	(b)	20.9	–	0.3	(2.9)	(0.8)	17.5
Other	(c)	–	1.8	–	–	–	1.8
		22.5	1.8	0.3	(2.9)	(2.4)	19.3

Analysis of total other provisions		2012 £m	2011 £m
Non-current		14.7	15.9
Current		4.6	6.6
		19.3	22.5

(a) The provision for reorganisation and restructuring principally relates to restructuring within corporate office functions.

(b) The provision for onerous contracts relates to retail property leases. The leases will expire over the period between 2013 and 2025.

(c) The other category comprises various provisions which are not individually sufficiently material to warrant separate disclosure.

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

48 LOANS AND OTHER BORROWINGS

Analysis by instrument and maturity	Notes	Interest rate*	Maturity	2012 £m	2011 £m
On demand loans with Iberdrola group companies		Base + 1%	On demand	130.8	40.8
Collateral		LIBOR	30 June 2013	39.1	47.9
£200 million euro-sterling bond	(b), (c)	8.375%	20 February 2017	199.4	199.2
£300 million medium-term note	(d)	5.9%	22 February 2021	294.6	293.9
£250 million euro-sterling bond	(b), (e)	6.75%	29 May 2023	248.2	248.1
£175 million inflation linked bond	(d)	3.494% x RPI	13 October 2024	252.0	243.8
10 billion JPY loan	(f)	4.6%	27 July 2029	83.4	101.0
£50 million medium-term note	(d)	5.75%	9 December 2039	50.0	50.0
£100 million medium-term note	(d)	6.375%	31 May 2041	100.0	100.0
				1,397.5	1,324.7

* Base - Bank of England Base Rate; LIBOR-London Inter-Bank Offer Rate; RPI - Retail Prices Index

Analysis of loans and other borrowings	2012 £m	2011 £m
Non-current	1,229.9	1,238.1
Current	(a) 167.6	86.6
	1,397.5	1,324.7

- (a) Current borrowings comprise loans with Iberdrola Group companies repayable on demand and collateral together with finance costs due to be amortised within one year, short term element of fair value hedge adjustments and the adjustments on discontinued fair value hedges due to be amortised within one year. This totalled £2.3 million (2011 £2.1 million).
- (b) These bonds contain a "Loss of licences" covenant that will require repayment of the outstanding amount should the UK group lose all its electricity licences (distribution, transmission and supply licences).
- (c) The Sterling bond due 2017 can be redeemed at any time by the company at the higher of principal amount or redemption price (as determined by HSBC Bank plc) giving 30 to 90 days' notice to the lender.
- (d) Scottish Power Limited and the company have an established joint US\$7 billion euro-medium term note programme. Scottish Power Limited has not issued under the programme. The company has in issue various notes in Sterling, which can be redeemed by the company with 30 to 90 days' notice in case of unfavourable and unavoidable changes in the UK tax laws impacting on the note payments.
- (e) The Sterling bond due 2023 can be redeemed at any time by the company at the higher of principal amount or redemption price (as determined by HSBC Bank plc) giving 30 to 45 days' notice to the lender.
- (f) The interest rate quoted above on the 10 billion JPY loan is fixed. This is changed to a variable rate by a cross currency swap.
- (g) The company has no undrawn committed borrowing facilities at 31 December 2012 (2011 nil).

49 DERIVATIVE FINANCIAL INSTRUMENTS

Analysis of derivative financial instruments – carrying value

	2012				2011			
	Assets		Liabilities		Assets		Liabilities	
	Current	Non-current	Current	Non-current	Current	Non-current	Current	Non-current
Hedging derivatives								
Exchange rate hedges								
Fair value hedge								
– Currency swap	0.7	32.7	–	–	0.7	50.3	–	–
Cash flow hedge								
– Foreign exchange rate	–	–	(0.1)	–	–	–	–	–
Total derivatives	0.7	32.7	(0.1)	–	0.7	50.3	–	–

50 TRADE AND OTHER PAYABLES

	2012 £m	2011 £m
Current trade and other payables:		
Payables due to Iberdrola group companies – trade	0.2	35.8
Payables due to Iberdrola group companies – interest	0.6	0.5
Trade payables	22.5	26.9
Other taxes and social security	3.8	2.4
Capital payables	8.4	3.0
Other payables	43.0	43.1
	78.5	111.7
Non-current other payables:		
Other payables	1.8	1.7
	1.8	1.7

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

51 COMPANY INCOME STATEMENT

As permitted by Section 408 of the Companies Act 2006, the company has not presented its own income statement. The company's income statement was approved by the Board on 25 June 2013. The profit for the financial year per the Accounts of the company was £1,114.4 million (2011 £185.1 million).

52 AUDITORS' REMUNERATION

The auditors' remuneration of the group is billed on a group basis and is not recharged to the company. Of the total group audit fee for the year ended 31 December 2012, £30,000 (2011 £30,000) related to the audit of the company Accounts. The total auditors' remuneration for the group is disclosed in Note 33 to the consolidated Accounts.

53 DIVIDENDS

	2012 pence per ordinary share	2011 pence per ordinary share	2012 £m	2011 £m
Interim dividend paid	–	11.5	–	200.0

54 RELATED PARTY TRANSACTIONS

(a) Transactions and balances arising in the normal course of business

	Related Party							
	2012				2011			
	Ultimate parent company (Iberdrola S.A.) £m	Ultimate UK parent (Scottish Power Limited) £m	Subsidiary companies £m	Other Iberdrola group companies £m	Ultimate parent company (Iberdrola S.A.) £m	Ultimate UK parent (Scottish Power Limited) £m	Immediate parent (Scottish Power UK Holdings Limited) £m	Other Iberdrola group companies £m
Types of transaction								
Sales and rendering of services	17.7	1.0	192.8	3.0	10.2	–	–	95.8
Purchases and receipt of services	(33.4)	(5.0)	15.5	–	(35.3)	(6.8)	–	(17.6)
Finance income	–	12.7	25.2	–	–	6.6	–	38.5
Finance costs	–	–	(1.1)	–	(0.1)	–	–	(1.6)
Dividends received	–	–	1,122.0	–	–	–	–	190.0
Dividends paid	–	–	–	–	–	–	(200.0)	–
Pensions contributions received	–	–	31.0	–	–	–	–	30.8
Acquisitions of subsidiaries (note (ii))	–	–	27.8	–	–	–	–	953.8
Disposals of subsidiaries (note (ii))	–	–	–	–	–	–	–	(660.5)
Balances outstanding								
Loans receivable	–	1,483.5	1,280.0	–	–	856.6	–	778.7
Trade receivables	17.5	–	3.3	14.5	16.0	–	–	11.6
Interest receivable	–	12.7	19.5	–	–	6.6	–	18.6
Loans payable	–	–	(130.8)	–	–	–	–	(40.8)
Trade payables	–	–	(0.2)	–	(35.4)	–	–	–
Interest payable	–	–	(0.6)	–	–	–	–	(0.5)

(i) The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received.

(ii) On 1 January 2012, as part of the Iberdrola group reorganisation, the group acquired certain renewable energy companies from another Iberdrola group company. On 1 July 2011, a group restructuring exercise took place to align the operational structure of ScottishPower with the operational structure of Iberdrola. Details of the transactions that the company participated in, in both years, are set out at Note 34.

(b) Remuneration of key management personnel

The remuneration of the key management personnel of the company is set out below. As all of the key management personnel are remunerated for their work for the Iberdrola group, it has not been possible to apportion the remuneration specifically in respect of services to this company. All of the key management personnel are paid by the company.

	2012 £m	2011 £m
Short-term employee benefits	0.6	0.9
Post-employment benefits	0.1	0.1
Share-based payments	0.2	0.3
	0.9	1.3

(c) Directors' remuneration

Details of directors' remuneration are set out at Note 32(c).

NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2012

54 RELATED PARTY TRANSACTIONS *continued*

(d) Ultimate parent company

The directors regard Iberdrola S.A. as the ultimate parent company, which is also the parent company of the largest group in which the results of the company are consolidated. The parent company of the smallest group in which the results of the company are consolidated is Scottish Power UK Holdings Limited. Copies of the consolidated Accounts of Iberdrola S.A. may be obtained from Iberdrola S.A., Torre Iberdrola, Plaza Euskadi 5, 48009, Bilbao, Spain. Copies of the consolidated Accounts of Scottish Power UK Holdings Limited may be obtained from The Secretary, Scottish Power UK Holdings Limited, 1 Atlantic Quay, Glasgow G2 8SP.

Scottish Power UK plc

Registered office: 1 Atlantic Quay, Glasgow G2 8SP

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