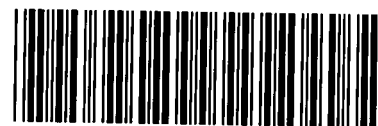




SCOTTISHPOWER

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COMPANIES HOUSE

Registered No. SC117120

SCOTTISH POWER UK PLC  
ANNUAL REPORT AND ACCOUNTS  
FOR THE YEAR ENDED 31 DECEMBER 2017

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Some of the statements contained herein are forward looking statements about Scottish Power UK plc and its subsidiaries, and Iberdrola, S.A.'s strategic plans. Although Scottish Power UK plc and Iberdrola, S.A. believe 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.

# STRATEGIC REPORT

The directors present an overview of Scottish Power UK plc's structure, 2017 performance, strategic objectives and plans.

## SCOTTISH POWER UK PLC GROUP STRATEGIC OUTLOOK AND 2017 PERFORMANCE

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 and distribution of electricity, energy management and the supply of electricity and gas principally in the United Kingdom ("UK"). The three segments reported by the group during the year were Energy Networks, Energy Wholesale and Retail, and Renewables. The company is a wholly owned subsidiary of Iberdrola, S.A. ("Iberdrola"), one of the largest utility companies in the world and the top renewable energy producer in Europe.

Scottish Power Limited is the UK holding company of the Scottish Power Limited group ("ScottishPower") of which the company is a member.

The group's strategic objectives include:

- investing to power the UK's economic future by optimising existing and future assets to deliver sustainable performance for customers and shareholders;
- making clean energy work for the UK to help fight climate change, including reducing the cost of offshore and onshore wind energy, encouraging the development of appropriate energy storage and investing in the group's networks to make them smarter and more resilient; and
- putting customers in control during the digital shift so that everyone has the opportunity to benefit from ScottishPower's affordable deals and recommended energy efficiency measures.

The macro-economic situation in the UK remains stable but it is characterised with uncertainty as the negotiations for the UK to leave the European Union ("EU") progress ahead of March 2019. The group is working with the UK Government to help shape the future of energy policy following "Brexit" with a view to mitigating any risks and developing opportunities. The group primarily operates in UK markets with some Renewables investment in the Republic of Ireland.

The UK Government has confirmed that an allocation of up to £557 million of funding will be available for Contracts for Difference ("CfD") auctions for renewable generation over the years to come. An auction is planned for the Spring of 2019, using some of that budget, which will provide opportunities for new offshore wind and certain other renewable projects. In networks, the current regulatory framework for transmission expires in 2021. In July 2017 The Office of Gas and Electricity Markets ("Ofgem") began to consult on the next settlement of price controls with this work expected to accelerate in 2018 to prepare for the next settlement based on the Revenue = Incentives + Innovation + Outputs ("RIIO") regime. In October 2017, the Department of Business, Energy and Industrial Strategy ("BEIS") published a draft bill to introduce a price cap for all customers on Standard Variable Tariffs ("SVTs") and other default tariffs. Pre-legislative scrutiny of the bill is expected to conclude in mid-2018 with passage of the bill through to Royal Assent dependent upon the timetable of parliamentary business. The group does not believe that the proposed price cap will help engage customers to find a better deal and will continue to work hard to reward its loyal customers by encouraging them on to competitive tariffs.

Depending on the evolution of the UK's energy policy, the group's plan to invest £7 billion in the UK in the five years to 2020 remains on course.

In Scotland, following the 2016 parliamentary elections and 2017 general election, the Scottish Government is focused on its 'Programme for Government'. This includes new commitments to establish a publicly owned energy company in Scotland by 2021 and to end the sale of new fossil fuel cars by 2032 in favour of electric vehicles. The Scottish Government has yet to confirm its view on whether or not (and if so when) to seek a second referendum on Scottish Independence.

Looking forward to 2018 and beyond:

- the Energy Networks business will invest around £3 billion until 2023 as it continues to operate under the price control mechanisms laid out in the RIIO regime. The High Voltage Direct Current ("HVDC") Western Link project was commissioned in December 2017, allowing some 900 megawatts ("MW") of power to flow; further work at Hunterston to bring the capacity up to 2,200 MW is expected to be completed during 2018;
- the retail market continues to be competitive. Energy Retail's response includes a clear focus to serve existing customers well, to encourage customers to engage in the market to be on the best deal for them and to put them more in control of their energy usage through the roll out of smart meters and the provision of innovative digital products;
- in Renewables, the construction of the East Anglia One offshore wind farm continues with first export expected in 2019; and
- Energy Wholesale will continue to improve the efficiency of current plant and evaluate investment opportunities for new plant, as well as to optimise returns through the market and capacity market auctions.

The table below provides key financial information relating to the group's performance during the year. Further detail is provided in the individual segment sections of the Strategic Report.

Financial key performance indicators ("KPIs")	Revenue*		Operating profit*		Capital investment	
	2017 £m	2016** £m	2017 £m	2016 £m	2017 £m	2016 £m
Scottish Power UK plc group	5,239.1	5,142.6	653.8	831.3	1,700.4	1,730.0

\* The group's revenue and operating profit as presented on page 32.

\*\* Restated (refer to Note 2 on page 35).

In the financial year revenues have increased by £97 million, primarily as a result of increased revenue within the Energy Wholesale and Retail segment which is partly offset by higher procurement costs.

Operating profit for the financial year was £654 million, a decrease of £178 million. This decrease mainly reflects the 2017 operating loss of the Energy Wholesale and Retail segment. This loss is due to lower domestic retail volumes, increased Energy Retail government obligations and costs associated with the smart metering roll out, as well as lower Energy Wholesale gross margins.

The group's continued commitment to the UK and European energy market is reflected by a capital spend of £1.7 billion in 2017, consistent with 2016. Capital investment is focused on the Energy Networks and Renewables segments. The planned 2018 capital investment is expected to be in the region of £1.6 billion.

## STRATEGIC REPORT *continued*

### ENERGY NETWORKS

#### SEGMENT DESCRIPTION AND OUTLOOK

Energy Networks owns three regulated electricity network businesses in the UK. These businesses are "asset-owner companies", holding the regulated assets and Electricity Distribution and Transmission Licences of the group, and are regulated monopolies. They own and operate the network of cables and power lines transporting electricity to around 3.5 million connected customers in the south of Scotland, Cheshire, Merseyside, North Shropshire and North Wales.

Up to 31 December 2017, SP Power Systems Limited ("Power Systems"), an unregulated business, provided asset management expertise and conducted the day-to-day operation of the networks. Along with the asset-owner companies it acted as an integrated business unit to concentrate expertise on regulatory and investment strategy, with Power Systems implementing programmes commissioned by and agreed with the asset-owner companies. Strict commercial disciplines were applied at the asset-owner service provider interface, with Power Systems operating as a contractor to the distribution and transmission businesses. From 1 January 2018, the role of Power Systems has changed and it now provides a narrower range of asset management support services as opposed to being an internal contractor delivering work programmes.

One of the regulated businesses, SP Transmission plc ("SPT") is a transmission network owner. The electricity transmission network consists of the high voltage electricity wires that convey electricity from power stations to distribution system entry points or, in certain cases, direct to end users' premises via a national network of high voltage grids.

The other two regulated businesses are Distribution Network Operators ("DNO"); SP Distribution plc ("SPD") and SP Manweb plc ("SPM"). The electricity distribution networks are regional grids that transport electricity at a lower voltage from the national grids and embedded generators to industrial, commercial and domestic users.

All three regulated businesses are natural monopolies and are governed by Ofgem via regulatory price controls. The primary objective of the regulation of the electricity networks is the protection of customers' interests while ensuring that demand can be met and companies are able to finance their activities. Price controls are the method by which the amount of allowed revenue is set for network companies over the period of the price control. Price control processes are designed to cover each company's efficient costs and allow them to earn a reasonable return, provided they act in an efficient manner, deliver value for customers and meet Ofgem targets.

The transmission and distribution network companies continue to face a considerable challenge to secure the significant investment required to maintain reliable and secure networks. To ensure that this investment is delivered at a fair price for customers, Ofgem introduced the RIIO framework. It is a performance based model, with eight year price control periods, that places a much greater emphasis on network companies playing a full role in developing a sustainable energy sector and delivering services that provide value for money for customers. A key feature is agreement on the set of outputs that companies are expected to deliver as part of the framework and the provision of incentives to reduce network costs for both current and future customers.

During 2017, SPT reached the half-way point in its transmission price control and the company's strong start has been maintained. The company is on track to complete an ambitious programme of network renewal. At March 2017, the company was almost 60% through its overhead line replacement programme of 870 km, being 312 km ahead of plan. Other major deliverables include the connection of five major onshore wind farms totalling 403 MW of directly connected generation, completion of two significant overhead line routes utilising innovative composite-core High Temperature Low Sag technology and completion of a cumulative 49% of non-load outputs, substantially ahead of the RIIO-T1 plan of 32% for the first four years. The HVDC Western Link project was commissioned in December 2017, allowing some 900 MW of power to flow; further work at Hunterston to bring the capacity up to 2,200 MW is expected to be completed during 2018.

In December 2017, SPT was awarded £4 million future revenue funding through the RIIO-T1 Environmental Discretionary Reward Scheme which focuses on strategic environmental considerations and organisational and cultural changes to facilitate growth in low carbon energy. SPT was the only transmission company to receive funding through this mechanism.

On 31 March 2017, SPD and SPM successfully completed the second year of the eight year price control RIIO-ED1 that will run until March 2023. Both companies are meeting or exceeding their regulatory targets which include a range of customer and stakeholder related outputs.

Energy Networks has recently achieved important milestones towards the goal of being a recognised leader in asset management. These include the signature of a corporate partnership with the Institute of Engineering and Technology ("IET") and Energy Networks' leading role in this year's CIREC (Congress International de Reseaux Electriques) conference in Glasgow, where Energy Networks' vision for evolution to a Distribution System Operator ("DSO") was well received.

In December 2017, SPM was awarded additional RIIO-ED1 future revenue funding of £24 million to manage an emerging public safety risk in relation to the replacement of low voltage network underground boxes. SPM was the only distribution company to receive additional funding through this mechanism.

During 2017 Energy Networks also won a number of awards:

- At the Utility Week Industry Awards the Stakeholder Engagement and Communications team received Utility Week Awards 2017 'Team of the Year'. Energy Networks won a record number of Utility Week Star Awards including 'Customer Service Process', 'Rising Star' and 'Hero Team'.
- At the Saltire Civil Engineer Awards, the Beauldy-Denny transmission project was awarded 'Great Contribution to Scotland'.
- For the third year in a row Energy Networks has received an award at the Scottish Green Energy Awards, with the award being for 'Sustainable Development' for FITNESS (an innovation project to reduce the carbon footprint of substations).
- At the prestigious National Planning Awards Energy Networks won 'Highly Commended' in the Sustainability Award category for involvement in nature work.
- At the Scotland Diversity Awards an employee progressing through Energy Networks' graduate scheme received the 'Rising Star' Award.

In line with the group's strategic objectives and its regulatory obligations, Energy Networks is maintaining its significant investment in the UK energy network. Over the last ten years, it has invested around £5.5 billion in its transmission and distribution networks, and during the next ten years, Energy Networks currently plans to invest a further £6 billion to modernise and improve service to customers. Energy Networks' ten year investment plans are reviewed annually in detail to ensure plans are aligned with, and continue to support, UK Government energy policy.

## STRATEGIC REPORT *continued*

### ENERGY NETWORKS *continued*

#### SEGMENT DESCRIPTION AND OUTLOOK *continued*

A new Network Asset Management System was introduced in 2018. This more fully utilises functionality within Energy Networks' existing SAP enterprise resource planning system. Key improvements targeted include standardised and streamlined business processes alongside automated work management and reporting.

Looking ahead, Energy Networks will continue to play a part in the roll out of smart meters. In some properties there is a requirement to upgrade Energy Networks' assets to enable the fitting of a smart meter or to respond to an emergency situation. Such interventions may continue to be required in greater numbers than previously forecast by the industry. As the deployment of smart metering increases, plans have been updated to ensure resource levels are adequate to meet the challenge.

In 2017, both the Scottish and UK Governments outlined plans to limit the purchase of new diesel or petrol vehicles after 2032 and 2040 respectively. To enable the wide scale roll out of electric vehicles ("EV"), it is key that the UK's electricity networks can facilitate suitable charging infrastructure for customers at a reasonable cost. Energy Networks will be engaging with a range of stakeholders to understand the capabilities of EV products and thereby understand the potential impact on customers' electrical needs.

Launched in January 2017, the Energy Networks Association Open Networks project lays the foundations of a smart energy grid in the UK. The project brings together the UK energy industry as well as leading academics, trade associations and non-governmental organisations and aims to transform the way networks work. The project will enable the UK's energy networks companies to move from the traditional role of delivering electricity in one direction from centralised power plants to homes and communities, to one where the network acts as a smart platform that enables a whole range of new energy technologies that generate, consume and manage electricity. The project is a key tool to support Energy Networks' vision to transition from a traditional DNO role to that of a DSO.

In November 2017, SPD was awarded £8 million future revenue funding through the RII0-ED1 innovation roll out mechanism to deploy an industry leading active network management scheme in Dumfries and Galloway. SPD was the only company to receive funding through this mechanism.

2017 was also a successful year for Network Innovation Competition submissions with both submitted projects being awarded funding by Ofgem. The SPD FUSION project, which seeks to demonstrate and implement open market tools to trial DSO concepts on the network, was awarded £5 million future revenue funding. The project is aligned with both Energy Networks' DSO vision and the Energy Networks Association Open Networks project. The SPM Low Voltage Engine project was awarded £7 million future revenue funding and will trial the introduction of a novel solid state transformer which could be a key tool in addressing network challenges of the future, for example the EV rollout.

Announcements in the past few years by the UK Government on funding programmes have led to some renewables developers scaling back future activity. Some developers have requested acceleration in connection dates, while other projects have been deferred or cancelled. These developments have been analysed carefully, resulting in updated projections of volumes and expenditure for the Energy Networks business. The external environment will continue to be monitored and the impact of any changes in trends will be considered in future forecasts. Investments in interconnectors moving energy across the UK, for which Scottish export capability was previously the main driver, have become important to ensure security of supply in Scotland through import capability, in light of large thermal plant closures on both sides of the Anglo-Scottish border.

Energy Networks is mindful that some of its assets are critical national infrastructure. Energy Networks liaises with UK Government agencies to ensure that any potential threats and risks are assessed and mitigated. Energy Networks takes steps to enhance both the physical security of its assets and the security of its associated IT and communications systems in circumstances where potential risks are identified.

Energy Networks is continuing to develop and train staff for a 'smarter' future and replenish its ageing workforce from the communities served so that the investment made in recruitment and training continues to deliver in the long-term. The challenge of replacing an ageing workforce in Energy Networks and across the UK Power Sector in the coming years will be significant. Energy Networks will continue to work closely with schools and Further and Higher Education institutions to ensure that it can attract high calibre individuals into exciting development and career opportunities. During 2017 Energy Networks recruited 13 Graduates, 8 Power Engineering Apprentices, 24 Apprentices and 12 Adult Craft Trainees, and in addition, internal recruits have been enrolled on the Trainee Engineer and Technical Craftsperson programmes to increase the engineering and technical capabilities of the front line teams.

#### 2017 OPERATIONAL PERFORMANCE

Financial key performance indicators ("KPIs")	Revenue *		Operating profit **		Capital investment ***	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Energy Networks	1,071.0	1,079.8	538.9	577.2	732.6	767.1

\* Segment total revenue as presented in Note 6 on page 50.

\*\* Segment operating profit as presented in Note 6 on page 51.

\*\*\* Segment capital investment as presented in Note 6 on page 53.

Energy Networks' revenue is £9 million lower than the prior year. Distribution volumes were £15 million lower in 2017 and allowable distribution revenues decreased under RII0-ED1. This was partly offset by the profile of allowable transmission revenues increasing under RII0-T1.

Operating profit decreased by £38 million to £539 million in 2017, due to lower revenues, increased property taxes and increased depreciation charges reflecting continued levels of investment.

Energy Networks' capital investment decreased by £35 million to £733 million in 2017, primarily due to decreased spend in SPT as a number of major projects near completion.

## STRATEGIC REPORT *continued*

### ENERGY NETWORKS *continued*

#### 2017 OPERATIONAL PERFORMANCE *continued*

The three regulated businesses within Energy Networks are required to prepare regulatory accounts for the years ending 31 March. Reporting of key performance indicators is aligned to the regulatory year end. Consequently, the latest available data for the last regulatory year for Energy Networks has been disclosed in the table below, with the exception of distributed energy that is reported for the years ending 31 December.

Non-financial key performance indicators	Notes	Actual 2017	Target 2017	Actual 2016	Target 2016
<b>Distributed energy (GWh)*</b>					
- SPD		17,749	N/A	18,181	N/A
- SPM		15,023	N/A	15,301	N/A
<b>Customer interruptions</b>	(a)				
- SPD		42.9	51.9	48.5	52.1
- SPM		38.2	38.1	30.2	38.3
<b>Customer minutes lost</b>	(b)				
- SPD		29.3	45.7	34.8	46.2
- SPM		37.3	44.2	33.6	45.6
<b>Customer Performance:</b>	(c)				
<b>Broader customer service measure – Interruptions</b>					
- SPD		8.74	8.20	8.79	8.20
- SPM		8.74	8.20	8.86	8.20
<b>Broader customer service measure – Connections</b>					
- SPD		8.43	8.20	8.36	8.20
- SPM		8.68	8.20	8.43	8.20
<b>Broader customer service measure – General enquiries</b>					
- SPD		9.05	8.20	8.84	8.20
- SPM		9.30	8.20	9.24	8.20
<b>Energy ombudsman (Customer complaints)</b>	(d)				
- SPD		5	–	2	–
- SPM		2	–	1	–
<b>Transmission operational performance (Incentivised incidents)</b>	(e)				
- SPT		4	–	4	–

\* Gigawatt hours ("GWh")

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

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

(c) Broader customer service measures are assessed using the following three methods; a customer satisfaction survey, complaints metric and stakeholder engagement.

(d) The Energy Ombudsman Services, an independent body, monitors and adjudicates complaint cases.

(e) Transmission operational performance is reported as the number of 'energy not supplied' and associated incidents. These incentivised incidents are incidents where the loss of supply is longer than three minutes.

Energy Networks is committed to maintaining high performance during extreme weather events. Consequently, during the course of the year over £70 million was invested to refurbish or rebuild sections of the overhead line network. In addition £13 million was invested in tree cutting activities. Both of these investments have contributed significantly to improving the performance of distribution assets during storms.

The long-term safety and reliability of Energy Networks' electricity distribution networks and their impact on customers are key business priorities. The networks are designed and operated in a way that ensures the safety of the public and employees with a minimal number and duration of supply interruptions.

## STRATEGIC REPORT *continued*

### ENERGY WHOLESALE AND RETAIL

#### SEGMENT DESCRIPTION AND OUTLOOK

Given the complexity of the Energy Wholesale and Retail segment and in the interests of transparency, analysis of the key business functions has been provided below.

#### ENERGY WHOLESALE

Energy Wholesale's operations are focused on managing the complex market conditions in relation to the operation of the group's generation asset base (except for those technologies managed by Renewables) and managing the group's exposure to the UK wholesale electricity and gas markets for both Generation and Retail.

Generation owns and operates 2,531 MW of generating capacity comprising gas and hydro-electric generation assets, giving the business a flexible and balanced portfolio. The coal-fired Longannet power station closed on 24 March 2016, resulting in 2017 being the first full year without any coal generation.

Energy Management is predominantly responsible for:

- the purchase of external supplies of gas and emissions allowances for the generation of electricity;
- the purchase of external supplies of electricity and gas for onward sale to customers;
- the optimisation of gas storage; and
- the sale of electricity to wholesale market participants in the UK.

Capacity market auctions are now the most important factor in making future strategic decisions, including building new plant, as well as optimising the existing portfolio. Energy Wholesale has a strong development portfolio containing strategic projects that, subject to market signals, will grow in the future.

Due to auction timings there was no T-4 capacity market auction in 2017. The T-4 auction for delivery in 2020/21 took place in December 2016, clearing at a price of £22.50 per kilowatt ("kW") while the T-4 auction for delivery in 2021/22 took place in February 2018, clearing at £8.40 per kW. This low price may reflect the entry of a number of new interconnectors, in competition with some existing coal units; the future trajectory of the auction clearing price is, at this stage, difficult to predict.

The group's existing portfolio of power stations, including gas, hydro-electric and pumped hydro storage, will receive revenues from the capacity market going forward, but any plant receiving funds from the Renewables Obligation or a CfD are excluded.

The continued significant cost reduction in both solar and wind technologies has highlighted the importance and value of flexibility in achieving long-term decarbonisation goals, and Energy Wholesale has an opportunity to extend the existing pumped hydro storage plant at Cruachan both in terms of generation and storage capacity. A key issue, however, is the uncertainty in the likely investment returns and whether a risk reduction mechanism can be put in place to address this.

Overall, Energy Wholesale's portfolio and strategic development options are well positioned to take advantage of future market conditions.

#### ENERGY RETAIL

Energy Retail is responsible for the supply of electricity and gas to domestic and business customers throughout Great Britain, as well as providing customer services such as customer registration, billing and receipting processes and handling enquiries in respect of these services. Energy Retail is also responsible for the associated metering activity and managing the group's Energy Services activities. During 2017, an average of 5.3 million gas and electricity customers were supplied by Energy Retail.

Energy Retail has continued to work with Ofgem to implement the remedies set out in the Competition and Markets Authority ("CMA") report. This includes continued engagement to support Ofgem in the development of the proposed domestic customer database of disengaged customers.

Following the results of the CMA investigation, the regulatory changes in the gas and electricity market in the UK have removed the restriction on suppliers to only have four tariffs available. Energy Retail has embraced this change by launching more personalised tariffs, open to both existing and new customers.

Domestic market switching reached record levels in 2017 according to Energy UK, showing a year on year increase of 15% versus 2016 levels. Energy Retail continues to outperform other major suppliers in terms of customer losses, and leads the way in having the lowest percentage of domestic customers on SVTs with well under half of non-prepayment customers now on SVTs.

During the Conservative Party Conference speech on 4 October 2017, Prime Minister Theresa May announced that the UK Government would consult on a bill requiring Ofgem to cap SVT and default tariffs; in effect putting a maximum price on the whole domestic market. Depending on the level of the cap, and whether the UK Government takes any mitigating actions, the measure is likely to have a negative impact on Retail's income and is potentially detrimental to competition and market engagement by consumers. The group is continuing to stress the benefits of a pro-competitive approach to customer engagement and SVTs, arguing that suppliers should be given targets to reduce SVT numbers, as well as seeking to ensure that the cap is set at an appropriate level and to encourage mitigating actions to be taken. Among these actions, the group will seek appropriate allowances for the rising cost of the smart metering programme and for the costs of customers, such as those with payment difficulty, who may be expensive to serve. The group will also seek to ensure that the competitive distortion caused by smaller suppliers being exempt from participating in the UK Government's fuel poverty and insulation programmes is addressed. Due to the time needed for the passage of the bill and the implementation process by Ofgem, the proposed price cap is unlikely to have a significant impact on revenues in 2018. Given that the group has the lowest proportion of customers on SVTs of the major suppliers, the impact of a proposed price cap will have less impact than on other major suppliers with a greater proportion of SVT customers.

Energy Retail is working hard to continually make improvements to its customer service. In recent years Energy Retail has focused its efforts on improving customer service processes including call centre operations and online services and in further enhancing the online experience for both existing and prospective customers, to give them greater freedom as to how they set up a new account or manage an existing account.

## STRATEGIC REPORT *continued*

### ENERGY WHOLESALE AND RETAIL *continued*

#### SEGMENT DESCRIPTION AND OUTLOOK *continued*

##### ENERGY RETAIL *continued*

The introduction of a number of innovative market-first digital services such as the Direct Debit Manager and the option for customers to make payments via an app on their mobile device, are helping customers to control their energy account and their interaction with Energy Retail. These digital tools provide an additional channel through which customers can more effectively manage their energy account, at a time that suits them. Energy Retail has also implemented a new online Customer Support Centre, which was set up in response to feedback from its customer panel and from the experience of its customer-facing teams. The Customer Support Centre uses innovative functionality to recognise the customer's account status, to allow Energy Retail to present each customer with information that is most relevant to them.

In addition to this, Energy Retail offers specific help to its most vulnerable customers:

- The ScottishPower Hardship Fund, which was launched in May 2015, has provided over £25 million in debt relief to customers in hardship.
- Energy Retail has also helped to refer around 7,500 customers to get help with ongoing budget and debt issues from its chosen free debt advice charity, National Debtline.
- Following changes to the supply licence, Energy Retail has made available to customer-facing staff new styles of vulnerable categories, such as those in temporary vulnerable situations. These will better help Energy Retail to support customers during periods of uncertainty.
- The ScottishPower Energy People Trust Fund ("the Trust") (an independent registered charity (SC036980)) funds other registered charities that help people whose lives are affected by fuel poverty. During 2017, the Trust awarded over £0.6 million to 17 projects, helping over 7,000 households (over 16,000 individuals). Since the Trust was established in November 2005, it has awarded over £15 million to 354 projects helping almost 2 million people in over 1 million households throughout Great Britain. This has resulted in an increase in household income of over £90 million. In addition 518 jobs were created and 709 volunteers supported these individuals. In light of ScottishPower's decision to consolidate its future charitable funding through the ScottishPower Foundation (a separate charity established in 2013), the Trustees resolved during 2017 to wind up the Trust upon the completion of all beneficiary projects, and the exhaustion of the Trust's funds within the next two years.

The delivery of energy efficiency measures continues to be an important responsibility of Energy Retail and 2017 was the fourth year of delivery of the UK Government's Energy Company Obligation ("ECO"). The ECO scheme focuses on reducing heating costs for the most vulnerable customers, and also aims to improve the energy efficiency of properties. Energy Retail continues to make strong progress towards delivering this obligation and has delivered a sufficient volume of measures to meet its March 2018 obligation targets. Energy Retail also supports vulnerable customers with their energy bills through the Warm Home Discount scheme ("WHD"); spending almost £40 million in 2017 providing assistance to over 214,000 customers.

Energy Retail continues to play its part in the roll out of smart meters and has made good progress in 2017 in mobilising and increasing its smart deployment capabilities, focusing on achieving the regulatory target of taking all reasonable steps to install a smart meter at 100% of premises by the end of 2020. Energy Retail has established a network of installers, who, together with Energy Retail's own metering teams, provide a strong platform to further increase its deployment capability for the remainder of the roll out.

#### 2017 OPERATIONAL PERFORMANCE

Financial key performance indicators ("KPIs")	Revenue *		Operating (loss)/profit **		Capital investment ***	
	2017 £m	2016**** £m	2017 £m	2016 £m	2017 £m	2016 £m
Energy Wholesale and Retail	4,272.8	4,196.3	(61.3)	151.7	208.2	115.7

\* Segment total revenue as presented in Note 6 on page 50.

\*\* Segment operating profit as presented in Note 6 on page 51.

\*\*\* Segment capital investment as presented in Note 6 on page 53.

\*\*\*\* Restated (refer to Note 2 on page 35).

Energy Wholesale and Retail revenue increased by £77 million to £4,273 million in 2017. This increase was primarily driven by higher volumes of industrial and commercial sales which have been largely offset by higher procurement costs.

Operating profit reduced by £213 million to an operating loss of £61 million in 2017. This reflected the impact of gross margin reductions (lower 2017 domestic volumes in Energy Retail and the 2016 favourable mark-to-market movements in relation to long-term gas contracts), as well as increases in smart metering costs associated with the roll out and in the government-levied WHD scheme costs. This was partially offset by the impact of lower operating costs and depreciation in Energy Wholesale following the closure of Longannet.

Capital investment increased by £93 million primary reflecting the 2017 investment to support the roll out of the smart metering programme.



## STRATEGIC REPORT *continued*

### ENERGY WHOLESALE AND RETAIL *continued* 2017 OPERATIONAL PERFORMANCE *continued*

Non-financial key performance indicators	Notes	2017	2016
<b>Plant output (GWh)</b>	(a)		
- Coal		–	1,636
- CCGT*		7,100	8,234
- CHP**		–	1
- Hydro and Other		692	585
		<b>7,792</b>	<b>10,456</b>
<b>Generating capacity (MW) as at 31 December</b>	(b)		
- Coal		–	–
- CCGT*		1,967	1,967
- CHP**		1	1
- Hydro and Other		563	563
		<b>2,531</b>	<b>2,531</b>
<b>Availability</b>	(c)	<b>89%</b>	<b>82%</b>
<b>Volume supplied (GWh)</b>		<b>51,105</b>	<b>52,925</b>
<b>Customer service performance</b>	(d)	<b>5th</b>	<b>6th</b>
<b>Customers (thousands)</b>	(e)		
- Electricity		3,170	3,218
- Gas		2,115	2,143
		<b>5,285</b>	<b>5,361</b>

\* Combined Cycle Gas Turbine

\*\* Combined Heat and Power plant

(a) Plant output is a reflection of the electricity generated by the business measured in GWh. CCGT plant output reduced due to planned major inspections in 2017.

(b) Generating capacity is the maximum output per second that generating equipment can supply to system load, adjusted for ambient conditions.

(c) Availability is the percentage of the year that the plant is available for use.

(d) Based on the Citizens Advice Domestic Energy Suppliers' Customer Service Report. Rankings reflect the group's position relative to the other 'Big Six' Energy Companies.

(e) Customer numbers are based on the average number of Meter Point Administration Numbers for electricity customers and Meter Point Reference Numbers for gas customers during the year to 31 December.

## RENEWABLES

### SEGMENT DESCRIPTION AND OUTLOOK

Renewables is responsible for the origination, development, construction and operation of renewable energy generation plants, predominantly onshore wind, with a large and growing presence in offshore wind, and the exploration of emerging renewable technologies and innovations such as battery storage.

Renewables has a successful track record as a developer of onshore wind farms with a conversion rate of MW capacity from planning to consent of over 90%. The business is the leading developer of onshore wind farms in the UK with a current onshore operating capacity of 1,907 MW.

Renewables continues to explore development opportunities for future growth onshore. This work includes publication during 2017 of reports highlighting the cost effectiveness of onshore wind under a market stabilisation CfD and the associated benefits of future onshore wind deployment in terms of local economic impact, job creation and community benefit.

Whilst no commitment has been made by the UK Government to offer CfD support for onshore wind in the future, UK Ministers have noted that they are considering options to bring forward onshore wind, particularly in areas of the UK that want to deploy it, noting it is an important part of the generation mix. The 2017 Conservative Manifesto was silent on CfD support, but did opine that there was a sufficiency of large onshore wind in England. The Scottish Government has reaffirmed its ongoing support for onshore wind as part of its Onshore Wind Policy Statement published in December 2017.

Renewables is also a leading developer and operator of offshore wind in the UK. The 389 MW West of Duddon Sands ("WODS") project in the East Irish Sea is a 50/50 joint arrangement with Orsted West of Duddon Sands (UK) Limited. Availability and production was ahead of expectations in 2017 with performance in 2018 set to be in line with expectations. Following the £2.5 billion Final Investment Decision ("FID") for its 714 MW East Anglia One project in early 2016, Renewables has placed all principal supply and installation contracts and the project is currently under construction, with first export scheduled in 2019. In August 2017, Renewables also received consent from the Secretary of State for BEIS for its 1.2 gigawatts ("GW") East Anglia Three offshore wind project and continues to make progress in relation to the remainder of the East Anglia Zone, with around 1.7 GW of projects at various stages of development. East Anglia Three is likely to be eligible to participate in the next CfD allocation round which the UK Government has suggested will take place in Spring 2019.

The UK Government's commitment to proceed with the 2019 CfD process follows the second CfD allocation round of September 2017 which delivered strike prices for projects set to deliver in 2022/23 at £57.50/MWh ("megawatt hour"), a 50% reduction against the previous CfD auction held in 2014. The UK Government has also confirmed its commitment that a sum of £557 million will be preserved for future allocation rounds in support of low carbon generation.

The UK Treasury's 2017 Autumn Budget confirmed that the levy control framework is to be discontinued beyond 2020/21 and that no further funds were expected to be made available for CfDs (beyond the £557 million referred to above) until the overall burden of low carbon generation support costs started to fall (probably after 2025). However, given the strike price achieved in the recent auction, the remaining £557 million could fund a large programme of offshore wind in the years to come as well, with potential to also support established technologies, such as onshore wind. The UK Treasury has also suggested that additional allocation pre-2025 could be considered if the overall effect is a net reduction in bills, which links to ongoing discussion regarding market stabilisation CfDs.

## STRATEGIC REPORT *continued*

### RENEWABLES *continued*

#### SEGMENT DESCRIPTION AND OUTLOOK *continued*

Renewables continues to engage with the UK Government on plans for future investments in renewable generation and the electricity system, including flexibility and energy storage.

Beyond the UK, on 1 August 2017, as part of a restructuring of Iberdrola's offshore wind portfolio, Renewables transferred its interest in projects in Germany and France to a related company within the Iberdrola group, Iberdrola Eólica Marina S.A.U. (refer to Note 36). Despite the sale of the legal entities, UK staff continue to be involved in the development of offshore wind projects in France and Germany, as well as in the United States of America.

#### 2017 OPERATIONAL PERFORMANCE

Financial key performance indicators ("KPIs")	Revenue *		Operating profit **		Capital investment ***	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
<b>Renewables</b>	<b>473.2</b>	<b>346.8</b>	<b>190.5</b>	<b>103.8</b>	<b>737.7</b>	<b>811.0</b>

\* Segment total revenue as presented in Note 6 on page 50.

\*\* Segment operating profit as presented in Note 6 on page 51.

\*\*\* Segment capital investment as presented in Note 6 on page 53.

Renewables revenue increased by £126 million to £473 million in 2017 due to higher electricity output mainly from increased average onshore operating capacity.

Operating profit increased by £87 million to £191 million in 2017 mainly as a result of increased revenue.

Capital investment decreased by £73 million to £738 million in 2017. UK based capital investment on onshore and offshore projects decreased by £25 million. Investment outside the UK decreased by £48 million mainly due to the Wiking offshore wind farm project in the Baltic Sea prior to its transfer (refer to Note 36).

Non-financial key performance indicators	Notes	2017	2016
Plant output (GWh)	(a)	4,178	3,098
Installed capacity (MW)	(b)	2,101	2,007
Availability	(c)	95%	96%

(a) Plant output is a measure of the electrical output generated in the year, which in turn drives the revenues of the business.

(b) Installed capacity represents the total number of MW fully installed within the wind farm sites. This includes all turbines erected irrespective of whether they are generating or not.

(c) Availability is a measure of how effective the business is at ensuring wind generating plant is available and ready to generate.

#### LIQUIDITY AND CASH MANAGEMENT

##### Cash and net debt

The group operates and manages a centralised cash management model within the UK with liquidity being centralised at the Scottish Power Limited level. The group's liquidity position and short-term financing activities are integrated and aligned with Iberdrola's.

The Iberdrola group objective is to retain sufficient liquid resources and facilities to cover anticipated cash flow requirements for a period in excess of twelve months; current liquidity in the Iberdrola group is in excess of £8 billion, which can be utilised if required to fund the group's activities.

Net cash flows from operating activities decreased by £389 million to £967 million for the year. As detailed in the table below, net debt decreased by £1,113 million to £5,057 million. Group loans payable decreased by £999 million while group loans receivable decreased by £112 million. Cash increased by £10 million to £46 million. External loans payable decreased by £216 million to £1,813 million.

Analysis of net debt	Notes	2017 £m	2016 £m
Cash	(a)	45.6	35.5
Group loans receivable	(b)	565.7	677.7
Group loans payable	(c)	(3,855.3)	(4,854.1)
External loans payable	(d)	(1,812.5)	(2,028.9)
<b>Net debt</b>		<b>(5,056.5)</b>	<b>(6,169.8)</b>

(a) As detailed on the consolidated balance sheet on page 30.

(b) As detailed in Note 12 on page 64.

(c) Loans with Iberdrola and other related Iberdrola group companies as detailed in Note 20 on page 72.

(d) External loans payable comprises external debt as detailed in Note 20 on page 72.

##### Capital and debt structure

The company is funded by a combination of debt and equity. All equity is held by Scottish Power Limited. The group's financing structure is determined by its position in the wider Iberdrola group. As stated above the group can obtain funding via the liquidity resources maintained at the Iberdrola group. The company holds investment grade ratings with Moody's Investor Services (Baa1), Standard & Poor's Rating Services (BBB+) and Fitch Ratings (BBB+). Details of the group's financial risk management policy are set out at Note 4.

On 5 October 2017, the company issued 2,640,000,000 ordinary shares of 50p each, to its immediate parent, Scottish Power Limited, for a total consideration of £1,320 million. The proceeds of the equity issuance were used to reduce the loans with other Iberdrola group companies.

## STRATEGIC REPORT *continued*

### TAXES AND OTHER GOVERNMENT OBLIGATIONS

To help give an understanding of the group's contribution to UK taxes and other UK Government obligations, the following table has been provided, highlighting the key taxes and other obligations in the financial year, on an accruals and cash basis.

Analysis of taxes and other government obligations	Notes	Income statement expense		Cash tax paid in the year	
		2017 £m	2016 £m	2017 £m	2016 £m
Carbon tax	(a)	52.2	85.6	55.6	88.9
Social security costs	(b)	30.1	28.1	30.7	30.0
Taxes other than income taxes	(c)	223.3	193.2	234.5	196.0
UK Corporation Tax	(d)	48.2	54.6	37.5	107.9
		353.8	361.5	358.3	422.8

(a) Carbon tax is a tax levied by the UK Government on the fossil fuels used to generate electricity. This is included within Procurements in the income statement.

(b) Social security costs as presented in Note 25 on page 74.

(c) Taxes other than income taxes as presented in Note 26 on page 75.

(d) UK Corporation Tax as presented in Note 30 on page 76.

### 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 the group. 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 the group maintained OHSAS 18001 Health and Safety Management System certification and began the process of recertification based on a stringent accredited approach which will align the group with the Iberdrola group approach.

The group's employee accident and incident statistics showed a decrease in 2017, and the incident severity remained low, however, consideration must be given to the contractor fatality which occurred on a Renewables contractor-managed project at Kilgallioch wind farm. Three employee lost time accidents\* were reported to the Health and Safety Executive ("HSE") under The Reporting of Injuries, Diseases and Dangerous Occurrences Regulations ("RIDDOR"). 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. The table below provides the occurrence of lost time accidents in each business.

Lost time accidents*	2017	2016
Corporate	–	–
Energy Networks	2	7
Energy Wholesale and Retail	1	–
Renewables	–	–
	3	7

\* Number of accidents involving the group's employees on the job resulting in the loss of at least a day's work.

Provision of public safety information and education about electricity safety has continued through delivery of a mixture of internet, community and school teaching programmes. As well as delivering safety education in schools, the group 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.

### UK DECISION TO LEAVE THE EU ("BREXIT")

The UK is scheduled to leave the EU on 29 March 2019. Following intensive negotiations on the subjects of a separation payment, mutual recognition of citizens' rights and avoiding a hard border between Northern Ireland and the Republic of Ireland, the UK and EU Commission negotiators published a Joint Report on 8 December 2017. This set out an agreed approach, allowing the European Council to conclude that sufficient progress had been made to move on to the next phase of discussions, which is expected to be agreement of a transition phase of around two years following Brexit where existing arrangements continue largely unchanged.

After agreeing the transition, it is intended that an ambitious trade deal will be negotiated, though the EU negotiators have indicated that the timetable is tight and the best that can be expected by March 2019 is a political declaration on the framework of the agreement.

Brexit may have both risks and opportunities for the group. Until the terms of exit and the nature of the future relationship are clear, it is not possible to be definitive about these. Many of the risks come from so-called "horizontal" issues where, if things go wrong in the negotiations, there could be issues affecting businesses in many sectors of the economy. These could include: restrictions on free movement (though the UK does give visas for skilled workers from non-EU jurisdictions); issues around data protection (though with the implementation of the General Data Protection Regulation, there may be sufficient UK/EU convergence to avoid a problem); the effect of any import tariffs on the supply chain for investments; and any impact on the overall strength of the UK economy (generally expected at present to be negative, at least for the short/medium-term). Variation in market views on this last factor is likely to manifest itself in movements (up or down) in the value of Sterling which is likely to have impacts on most group businesses, except to the extent that these can be hedged.

In terms of specific energy impacts, Brexit risks for the group appear low and there may indeed be some opportunities. UK generators are subject to competition from interconnector imports, which do not have to incur a number of grid charges that UK generators face and are also not affected by the Carbon Price Support tax. To the extent that Brexit uncertainty delays the growth in interconnection, or that these rules change over time, this could reduce the disadvantage suffered by UK generators. Any costs or savings from consequent changes in the wholesale market price are likely to be passed to consumers.

In terms of carbon pricing, the 2017 Budget announced that the sum of the Carbon Price Support tax and the EU Emissions Trading Scheme ("EU ETS") price would be maintained at a level similar to the current position until unabated coal was no longer used, regardless of whether or not the UK continued to participate in EU ETS. Late in 2017, a problem emerged as to whether the EU would recognise 2018 EU ETS allowances given Brexit. However, a solution was found in discussions between the UK and EU that will allow EU ETS to operate as normal in 2018. A further agreement will be required for 2019 in due course.

## STRATEGIC REPORT *continued*

### PRINCIPAL RISKS AND UNCERTAINTIES

ScottishPower's strategy, and so that of 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.

During 2017, 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 ("the Board"). ScottishPower's business risk assessment team and independent group Risk Management function supported the 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 business risks are adequately assessed, monitored, mitigated and managed. Further details of ScottishPower's governance structure and risk management are provided in Note 4 to the Accounts.

The principal risks and uncertainties of ScottishPower, and so that of the group, that may impact current and future operational and financial performance and the management of these risks are described below:

SCOTTISHPOWER – GLOBAL	
RISK	RESPONSE
Material deterioration in the relatively stable and predictable UK regulatory and political environment, including any sudden changes of policy, or interventions outside established regulatory frameworks.	Positive and transparent engagement with all appropriate stakeholders to ensure that long-term regulatory stability and political consensus is maintained and public backing is secured for the necessary investment in the UK energy system. Providing stakeholders with evidence of the risks of ad hoc intervention in markets.
Impacts arising from the UK decision to leave the EU or market reactions to events during the negotiation. These impacts could include movements in the value of Sterling and other financial instruments. In the longer term there could be negative or positive changes in the UK economy and in the political and regulatory environment in which ScottishPower operates.	In addition to monitoring ongoing developments related to "Brexit" a treasury risk management policy is in place to hedge financial risks which are the most prevalent in the short-term. Any longer term impact on the UK economy and its impact on ScottishPower and specific business units will be managed in line with developments.
A major health and safety incident in the course of operations could impact staff, contractors, communities or the environment.	ScottishPower's Health and Safety function provides specialist services and support for the businesses in relation to health and safety. A comprehensive framework of health and safety policy and procedures, alongside audit programmes, is established throughout ScottishPower, which aim to ensure not only continuing legal compliance but also drive towards best practice in all levels of its health and safety operations.
Breach in cyber security and unwanted infiltration of the ScottishPower IT infrastructure by internal and external parties.	Implementation of a cyber-risk policy which provides the framework for mitigation. Proactive approach to identifying where ScottishPower is vulnerable and addressing these points through technical solutions. Educating company employees as to how behaviour can reduce this risk. Embedding cyber security in all projects where appropriate.

## STRATEGIC REPORT *continued*

### PRINCIPAL RISKS AND UNCERTAINTIES *continued*

ENERGY NETWORKS	
<b>RISK</b> Failure to deliver the Distribution and Transmission outputs agreed with Ofgem in their respective price controls.	<b>RESPONSE</b> Mitigating actions include formulating detailed investment, resource, outage and contingency plans supported by an extensive procurement strategy. Good communication and co-ordination of activities across the business is integral to success, complemented by a comprehensive monitoring regime that provides early warning of potential issues.
Security of Supply due to potential asset failures alongside reduced generation capacity.	Risk based asset investment programme in place, business continuity and emergency planning well established including Black Start. "Strategic Spares" policy in place.
Failure to protect customer service performance.	Well-established customer service processes to respond to power loss, including storm readiness. Priority Service Register to protect vulnerable customers in the event of power loss. Implementation of a single emergency number to route customer queries.
Inability to recruit or retain an appropriately skilled workforce.	A Strategic Work Force Planning and Implementation plan that incorporates: a) retirement profiles with demographics; b) one year ahead Strategic Recruitment; and c) ten year Strategic Recruitment plan. Identification of business critical roles and succession planning.
Failure to respond to customers' changing requirements and to deploy new technologies through low carbon transition, for example electric vehicles, distributed generation, storage and heat pumps.	Mitigating actions include owning a clear DSO vision and influencing developments at industry forums, undertaking scenario modelling of the impact of low carbon technologies, considering technical and commercial innovation projects and lobbying key stakeholders.

## STRATEGIC REPORT *continued*

### PRINCIPAL RISKS AND UNCERTAINTIES *continued*

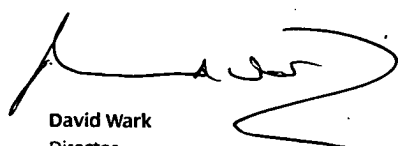
ENERGY WHOLESALE AND RETAIL	
RISK	RESPONSE
Risk of unfavourable results from capacity auctions, adversely affecting the returns from generation assets.	Optimising returns from the energy market and efficient control of costs, to maximise the chance of success in the auctions. Engagement with all relevant stakeholders to seek to ensure that the auctions are not distorted by hidden subsidies or loopholes in the auction design.
Adverse wholesale price movements and reduced energy market liquidity, adversely affecting the returns from generation assets.	Trading activity to secure value of assets and deliver return based on expected price movements, and providing support to Ofgem initiatives to stimulate liquidity.
The potential for plant performance issues reducing availability.	Technical assessments of key risk areas of operational performance, an optimised approach to repairs and maintenance and plans specific to each plant.
The introduction of a price cap for SVT customers, at an inappropriate level or in a way that distorts competition.	Continued focus on encouraging competition and promoting the use of fixed-price products; ongoing dialogue with lobbying of government and regulatory bodies to mitigate the risk.
Reduction in retail margins as a result of increasing non-energy costs, reduced market share and unfavourable wholesale energy costs.	Continued focus on improving customer service to enhance customers' experience; creating innovative, competitive products that compliment current offerings; increasing customer awareness of the ScottishPower brand; and improve efficiencies across the business through the new billing system.
The potential for non-compliance with the UK Government's mandate to complete the roll out of smart metering to customers in accordance with prescribed timescales.	Dedicated project team focused on ensuring adequate business processes and systems are developed. The team is responsible for ensuring the roll out capability is secured to enable deployment of meters. Energy Retail is an active participant in industry bodies responsible for developing smart metering technology and capability across the UK.
Reputational risk from customer service performance.	Continued investment in additional resource and employee training to handle customer queries and respond to complaints. Further mitigating actions include continued enhancement to key processes, including investment in the Energy Retail customer website.

## STRATEGIC REPORT *continued*

### PRINCIPAL RISKS AND UNCERTAINTIES *continued*

RENEWABLES	
RISK	RESPONSE
Changing energy policy in the UK with regard to renewable generation, particularly long-term decarbonisation objectives, coupled with affordability concerns presenting competition and allocation risk.	Actions to reduce allocation risk, including engagement with the UK Government regarding access and parameters of the CfD mechanism. Working to optimise Renewables' portfolio of assets and approach to development to ensure high performing and competitive assets will be able to participate in future auctions.
The potential for plant performance issues reducing availability.	Proactive technical assessments and monitoring of key risk areas associated with wind turbine performance, diversification of the service and maintenance model where reliance is placed on framework agreement for key activities, optimising service and maintenance activities to ensure each activity is appropriate based on operational knowledge. In addition, co-ordination with the procurement team in negotiating terms and conditions with turbine suppliers and independent operations and maintenance service providers to ensure plant performance is optimised.
Delivery of large and complex offshore projects on time and on budget.	ScottishPower and Iberdrola have a strong track record in delivering large scale engineering projects and have gained significant experience from developing the WODS and Wiking offshore wind farms. Risks are further reduced by using established and experienced suppliers and advisors along with robust financial management including appropriate foreign exchange hedging.
Identification and optimisation of future onshore development pipeline.	Engagement with national and local government to influence and inform policy regarding the role of onshore wind (including life extension and repowering), particularly in Scotland, in the future generation mix to ensure optimal levels of deployment.

BY ORDER OF THE BOARD



David Wark  
Director  
27 April 2018

## DIRECTORS' REPORT

The directors present their report and audited Accounts for the year ended 31 December 2017. References to 'ScottishPower' below apply fully to 'the group'.

### INFORMATION CONTAINED WITHIN THE STRATEGIC REPORT

The directors have chosen to disclose information on the following, required by the Companies Act 2006 to be included in the Directors' Report, within the Strategic Report, found on pages 1 to 13:

- information on financial risk management and policies; and
- information regarding future developments of the business.

### RESULTS AND DIVIDEND

The net profit for the year attributable to the equity holder of the parent amounted to £425.9 million (2016 £580.9 million as restated). A dividend of £300.0 million was paid during the year (2016 £663.0 million).

### TAXATION

The Board of Directors of Iberdrola has explicitly acknowledged its responsibility for tax policy and strategy in all of the companies that it controls. The Iberdrola Board has approved a Corporate Tax Policy which forms part of the Corporate Governance System and sets out that Board's commitment to responsible tax practices throughout the Iberdrola group. The Corporate Tax Policy was initially approved by the Iberdrola Board in 2010 and is regularly updated.

The Board of Directors of Scottish Power Limited (the group's parent company) has adopted this Corporate Tax Policy and its Audit and Compliance Committee has approved the ScottishPower Tax Strategy which accords with the Policy and, as required by UK law, is published on the ScottishPower website. This can be found at: [www.scottishpower.com/pages/tax\\_strategy.aspx](http://www.scottishpower.com/pages/tax_strategy.aspx).

ScottishPower is a responsible tax payer and seeks to be open, honest and transparent in dealings with the tax authorities and to comply with both the letter and the spirit of tax laws set by the UK Government. ScottishPower remits taxes due on a timely basis, and has a relationship with HM Revenue & Customs ("HMRC") based on mutual trust and cooperation. Payment of taxes is ScottishPower's principal contribution to sustaining public expenditure and one of its contributions to society.

Further details on taxes and other government obligations can be found in the Strategic Report on page 9.

### RESEARCH AND DEVELOPMENT

ScottishPower is aware of the importance of innovation to develop an industrial project at the vanguard of the sector. ScottishPower's research and development ("R&D") efforts are aimed at the optimisation of operational performance, improving security and reducing the environmental impact of its activities. All R&D is developed as part of Iberdrola's global open and decentralised R&D model.

ScottishPower's main areas of development during the past year have been focused on the Renewables' offshore development, smart grids and smart meter roll-outs, improving customer engagement and service, and the increase in network performance and availability. Detailed information in relation to ScottishPower's wider R&D activities can be found in the Iberdrola Innovation Report. The most recent report can be accessed via the 'Sustainability' section of [www.iberdrola.com](http://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. ScottishPower has developed an Integrated Environmental Management System (certified in accordance with ISO 14001:2004) that covers its operating business activities (CCGT, hydro and renewable generation, transmission and distribution of electricity, asset management and corporate areas). The organisation has successfully maintained its certification in line with ISO14001: 2004 via external audits in 2017, with the transition to a revised standard (ISO14001: 2015) due by August 2018. 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 can be found in the Iberdrola Sustainability Report. The most recent report can be accessed via the 'Sustainability' section of [www.iberdrola.com](http://www.iberdrola.com).

Further information on applicable environmental regulations is available on request from the Company Secretary.

### EMPLOYEES

The group had 6,066 employees at 31 December 2017 (2016 6,073). Of these, 3,014 (2016 2,857) were employed in Energy Networks, 2,154 (2016 2,405) in Energy Wholesale and Retail and 367 (2016 312) in Renewables, with the remaining 531 (2016 499) employed in Corporate services. During December 2017, costs of £38.1 million were recognised in the income statement following an announcement of a group wide efficiency programme. Refer to Note 25 for further details.

#### *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, grievance, harassment, discrimination, stress, anti-bribery and 'whistleblowing' and have been brought together in the Code of Ethics of Iberdrola and its group of companies (which also outlines expectations for employees' conduct).

#### *Training*

ScottishPower has a continuing commitment to training and personal development for its employees with over 2,900 (2016 2,700) training events and over 178,000 hours of training undertaken in 2017 (2016 139,000 hours). Much of the training is focused on health and safety and technical training ensuring field staff are safe and competent. In addition ScottishPower recruits over 100 craft and engineering trainees annually who undertake a formal structured training programme leading towards a recognised apprenticeship or formal engineering qualification. Team leaders and managers also participate in core management skills training and there are management development programmes and modules aimed at increasing our leadership capability.



## DIRECTORS' REPORT *continued*

### **EMPLOYEES** *continued*

#### **Employee feedback and consultation**

Employee feedback is recognised as key to driving engagement within ScottishPower and in 2017 the group again carried out its annual employee engagement survey, 'The LOOP'. The response rate in 2017 was in line with 2016 with 75% of employees across the group providing feedback. The overall engagement score increased to 79% in 2017 which is the highest ever level of engagement for ScottishPower and a positive reflection of how employees feel about working for the company. The results also show that ScottishPower's levels of engagement are in line with global utility peers.

All ScottishPower businesses recognise the importance of taking action in response to employee feedback and action plans are developed across the group. At a ScottishPower level, health and safety, image and reputation are areas of strength and employee feedback confirms that leadership, customer focus and personal development are the most important areas for employees.

In addition to employee feedback, ScottishPower regularly consults with employees and their representatives via a variety of channels, including monthly team meetings, business conferences, health and safety committees and employee relations forums.

#### **Equality and inclusion**

ScottishPower recognises the importance of difference and respects individuality as part of its ongoing commitment to promoting equality and inclusion. ScottishPower also understands that diversity goes beyond legally compliant policies and practices and includes a focus on creating an innovative, integrated organisation where people feel valued, inspiring them to perform at their best.

ScottishPower complies with The Equality Act 2010 and has published its gender pay gap information, based on data as at 5 April 2017, on its website.

ScottishPower has a Diversity and Inclusion Governance Group whose objective is to drive the Diversity and Inclusion action plan with key stakeholders across the organisation to ensure that diversity is embedded into ScottishPower's working policies and practices. Activities during 2017 included e-learning and training on diversity and unconscious bias to raise the awareness amongst management and employees.

ScottishPower is committed to driving gender diversity in the energy sector by encouraging women into leadership roles and engineering careers, not only seeking to develop its diverse and inclusive workforce but take active steps to address the deepening skills shortage in the sector. ScottishPower partners with external organisations such as the Women's Engineering Society and Powerful Women, and continues to sponsor and support industry initiatives such as the Top 50 Women in Engineering list and International Women in Engineering Day.

#### **Employment of disabled persons**

In support of the policy on Equality and Diversity (above), ScottishPower expects all employees to be treated with respect and has supporting policy guidance on People with Disabilities and Reasonable Adjustments to help ensure equality of employment opportunity for people with disabilities. The aim of these guidelines is to establish working conditions that 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.

#### **Employee health and wellbeing**

ScottishPower promotes and supports the physical and mental health and wellbeing of its employees through a programme of health promotion and information run by its occupational health department.

#### **Employee volunteering**

ScottishPower prides itself in being a good corporate neighbour, providing support to the communities it serves in each of its businesses. Volunteering is central to community involvement and ScottishPower has an excellent track record in this area. ScottishPower's company-wide Volunteering Policy has been actively utilised by employees during 2017. This policy gives all registered volunteers, on an annual basis, an opportunity to take an additional one day's paid leave, to be used as a volunteering day.

#### **Modern slavery statement**

ScottishPower is committed to human and labour rights and to eliminating modern slavery that could in any way be connected to its business. ScottishPower welcomed the introduction of the Modern Slavery Act 2015 and published its own Modern Slavery Statement which was approved by the Board of Directors of Scottish Power Limited. ScottishPower's Modern Slavery Statement is published on the ScottishPower website at: [www.scottishpower.com/pages/scottishpowers\\_modern\\_slavery\\_statement.aspx](http://www.scottishpower.com/pages/scottishpowers_modern_slavery_statement.aspx).

### **COMMUNITY RELATIONSHIPS**

#### **Community relationships**

Building the trust of communities has been part of ScottishPower's core values for many years. ScottishPower has a significant presence in many communities and aims to conduct its activities responsibly, in a way that is considerate to local communities and makes a positive contribution to society.

#### **Community consultation**

ScottishPower engages with communities across its operations, where both new and modernising developments are planned or where ScottishPower is decommissioning redundant or non-operational assets. The key areas where ScottishPower's business interacts with the community include the siting of new facilities such as wind farms, the presence of distribution and transmission lines, decommissioning older plant and routine maintenance and upkeep work. ScottishPower takes a proactive approach to providing good and accurate information from pre-planning through to construction.

ScottishPower maintains strong relationships with local communities by working with community groups, elected representatives, interest groups and individuals ensuring that those affected by the work are aware of what is happening in their area in advance, allowing communities to have their say. This is of particular importance to the business as a developer, owner and operator with longstanding relationships in many of the communities in which it works.

## DIRECTORS' REPORT *continued*

### COMMUNITY RELATIONSHIPS *continued*

#### *Community consultation continued*

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 such as Public Information Days and the publication of information on the ScottishPower website and social media outlets. ScottishPower's facilities 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.

As many of ScottishPower's assets, such as wind farms and pylons, are situated on land not owned by ScottishPower, 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, the local community and the general public. Energy Networks and those working on its behalf adhere to a Grantor's Charter which sets out guidance of commitment to grantors and has been prepared in consultation with key stakeholders.

Energy Networks has shaped its business around geographical districts, enabling them to get closer to the communities they serve and allowing local communities to have unprecedented influence upon the delivery of network projects in their area. A wide range of local partnerships have been developed to gain a better understanding of community needs, including vulnerability and to increase resilience in the communities served, whilst maintaining focus on excellent customer service. Strong engagement is placed at the heart of decision making at all levels of the organisation, winning the trust of communities and stakeholders.

#### *Investing in the community*

ScottishPower 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 volunteering and community based programmes. Opportunities are created for local employment during construction and operations through events such as "Meet the Developer" days where local contractors are invited to find out about opportunities at the group's facilities. The group works closely with the UK and devolved administrations to develop policy on community engagement and benefit and to ensure that ScottishPower adheres to all voluntary codes of good practice.

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 2017, ScottishPower voluntarily contributed £12.3 million (2016 £11.8 million) in community support activity of which £7.8 million (2016 £7.4 million) was contributed to registered charitable organisations. The £12.3 million (2016 £11.8 million) total incorporated £0.5 million (2016 £0.5 million) in management costs, £nil (2016 £0.1 million) categorised as charitable gifts, £6.6 million (2016 £6.8 million) categorised as community investment and £5.2 million (2016 £4.4 million) categorised as commercial initiatives; given in cash, through staff time and in-kind donations. Included within these figures, Renewables made £3.6 million (2016 £3.5 million) in voluntary community benefit payments to the communities neighbouring its wind farms.

These figures are compiled from ScottishPower's Community Investment Database, and are submitted annually in a return to LBG. The figures provided above will form part of the company's return in 2018 and have not yet been audited by LBG.

#### *ScottishPower Foundation*

ScottishPower established the ScottishPower Foundation to reinforce ScottishPower's commitment to charitable work throughout the UK. The ScottishPower Foundation is a registered Scottish charity (SC043862) and a company limited by guarantee (SC445116). Registered Office: 320 St. Vincent Street, Glasgow, G2 5AD. It provides funds to support charitable initiatives that promote the advancement of education, environmental protection, citizenship and community development, arts, culture and science as well as the prevention of poverty or disadvantage.

### POLITICAL DONATIONS AND EXPENDITURE

ScottishPower 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 2017, the group paid a total of £23,020 (2016 £22,010) for the sponsorship of conferences and events – activities that may be regarded as falling within the terms of the Act.

The recipients of these payments were:

- |                               |                      |
|-------------------------------|----------------------|
| • The Conservative Party      | £7,000 (2016 £7,000) |
| • The Labour Party            | £7,000 (2016 £7,000) |
| • The Scottish National Party | £9,020 (2016 £8,010) |

The above amounts were for sponsored receptions at the 2017 conferences of the above parties. 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 and were open to everyone attending the conference, including party members, non-governmental organisations, the media and trade unions. The payments do not indicate support for any particular party.

## 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 guiding principle, ScottishPower, and so the group, adopts the principles and rules contained in the most widely recognised good governance recommendations and, in particular, has taken as a reference (for guidance purposes only) the Uniform Good Governance Code for Listed Companies approved by the National Securities Market Commission of Spain. The company is not, however, subject to any corporate governance codes and, in particular, is not subject to the Uniform Good Governance Code for Listed Companies.

#### Administrative, management and supervisory bodies

##### *Board and management meetings*

The company is governed by a Board, consisting of three directors (refer to page 21) 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 Management Committee is a permanent internal body, without executive function, which was established by the Scottish Power Limited Board ("ScottishPower Board") to provide a coordinating role for activities of ScottishPower. The Management Committee meets weekly 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 assists the Chief Corporate Officer ("CCO") in the performance of his duties. The Management Committee comprises the following executives: the CCO (who was also Chief Executive Officer ("CEO") of the Renewables business until February 2018 when he became CEO of ScottishPower, which replaced the previous CCO role); the directors of Control and Administration, Regulation, Human Resources, UK Purchasing and Communications; the CEO of the Liberalised Business (Energy Wholesale and Retail); the CEO of the Regulated Business (Energy Networks); the CEO of the Renewables business; and the Head of Legal and General Secretary.

The Boards of Scottish Power Energy Networks Holdings Limited ("SPENH"), Scottish Power Generation Holdings Limited ("SPGH") and ScottishPower Renewable Energy Limited ("SPREL") are responsible for the effective management of the Regulated, Liberalised 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 comprised the Chairman Armando Martínez Martínez and six other directors as at 31 December 2017. The directors and their attendance at SPENH Board meetings held during the period under review (five meetings) are shown below:

Armando Martínez Martínez (Chairman)	Attended all meetings
Frank Mitchell (Chief Executive Officer)	Attended all meetings
Nicola Connelly	Attended no meetings (resigned 1 February 2017)
Antonio Espinosa de los Monteros	Attended all meetings
José Izaguirre Nazar	Attended all meetings
Scott Mathieson	Attended all meetings
Wendy Barnes (Independent non-executive director)	Attended all meetings
Elizabeth Haywood (Independent non-executive director)	Attended all meetings (resigned 31 December 2017)
Suzanne Fox (Independent non-executive director)	Attended one meeting (appointed 20 September 2017)

The terms of reference of the SPENH Board are published at:

[www.scottishpower.com/userfiles/file/SPENH-Terms%20of-Reference-Board-Directors-130603.pdf](http://www.scottishpower.com/userfiles/file/SPENH-Terms%20of-Reference-Board-Directors-130603.pdf).

##### *SPGH Board*

The SPGH Board comprised the Chairman Aitor Moso Raigoso and five other directors as at 31 December 2017. The directors and their attendance at SPGH Board meetings held during the period under review (five meetings) are shown below:

Aitor Moso Raigoso (Chairman)	Attended all meetings
Neil Clitheroe (Chief Executive Officer)	Attended all meetings
Heather Chalmers	Attended all meetings
Ángel Chiarri Toscano	Attended three meetings (resigned 3 October 2017)
Óscar Fortis Pita	Attended all meetings
Félix Rojo Sevillano	Attended all meetings
Gregorio Relaño Cobián	Attended two meetings (appointed 3 October 2017)

The terms of reference of the SPGH Board are published at:

[www.scottishpower.com/userfiles/file/SPGHL-Terms-of-Reference-Board-Directors-140224.pdf](http://www.scottishpower.com/userfiles/file/SPGHL-Terms-of-Reference-Board-Directors-140224.pdf).

## DIRECTORS' REPORT *continued*

### CORPORATE GOVERNANCE *continued*

#### Administrative, management and supervisory bodies *continued*

##### **SPREL Board**

The SPREL Board comprised the Chairman Xabier Viteri Solaun and five other directors as at 31 December 2017. The directors and their attendance at SPREL board meetings held during the period under review (five meetings) are shown below:

Xabier Viteri Solaun (Chairman)	Attended all meetings
Keith Anderson (Chief Executive Officer)	Attended all meetings
Jonathan Cole	Attended all meetings
Javier García de Fuentes Churrua	Attended all meetings
Unai Astiz Barrenetxea	Attended four meetings (resigned 26 October 2017)
Rafael de Icaza de la Sota	Attended one meeting (appointed 26 October 2017)
Lena Wilson (Independent non-executive director)	Attended one meeting (appointed 29 November 2017)

During February 2018, following an internal organisational restructure, Keith Anderson became the CEO of ScottishPower and Lindsay McQuade became CEO of Renewables.

The terms of reference of the SPREL Board are published at:

[www.scottishpower.com/userfiles/file/Renewables-ToRs-Board-Directors-130603.pdf](http://www.scottishpower.com/userfiles/file/Renewables-ToRs-Board-Directors-130603.pdf).

##### **ScottishPower Board**

The ScottishPower Board comprised the Chairman José Ignacio Sánchez Galán and seven other directors as at 31 December 2017. José Ignacio Sánchez Galán is also the Chairman and Chief Executive Officer of Iberdrola.

The directors of Scottish Power Limited are shown below:

José Ignacio Sánchez Galán	Chairman
Lord Kerr of Kinlochard GCMG	Vice Chairman, Independent non-executive director
Juan Carlos Rebollo Liceaga	
José Sainz Armada	
Keith Anderson	
Professor Susan Deacon	Independent non-executive director (resigned 1 July 2017)
Sir Tom Farmer CVO CBE KCSG	Independent non-executive director (resigned 1 July 2017)
Professor Sir James McDonald	Independent non-executive director
Dame Nicola Brewer	Independent non-executive director (appointed 11 July 2017)
Anthony Gardner	Independent non-executive director (appointed 11 July 2017, resigned 19 February 2018)

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

José Ignacio Sánchez Galán	Attended all meetings
Lord Kerr of Kinlochard GCMG	Attended all meetings
Juan Carlos Rebollo Liceaga	Attended all meetings
José Sainz Armada	Attended all meetings
Keith Anderson	Attended all meeting
Professor Susan Deacon	Attended two meetings
Sir Tom Farmer CVO CBE KCSG	Attended two meetings
Professor Sir James McDonald	Attended all meetings
Dame Nicola Brewer	Attended three meetings
Anthony Gardner	Attended two meetings

##### **ScottishPower Audit and Compliance Committee ("SP ACC")**

The SP 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 Articles of Association of Scottish Power Limited and by the terms of reference of the SP ACC. The SP ACC's responsibilities include:

- monitoring the financial reporting process for ScottishPower;
- monitoring the effectiveness of the ScottishPower's internal control, internal audit, compliance and risk management systems;
- monitoring the statutory audit of the Annual Report and Accounts of ScottishPower; and
- monitoring the independence of the external auditor and recommending to the ScottishPower Board the appointment or reappointment of the auditor and the associated terms of reference.

The SP ACC's terms of reference are published at:

[www.scottishpower.com/pages/audit\\_and\\_compliance\\_committee.aspx](http://www.scottishpower.com/pages/audit_and_compliance_committee.aspx).

##### **Membership and attendance**

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

Professor Sir James McDonald (Chairman)	External independent, attended all meetings
Professor Susan Deacon	External independent, attended two meetings (resigned 1 July 2017)
Juan Carlos Rebollo Liceaga	Attended four meetings
Anthony Gardner	External independent, attended two meetings (appointed 11 July 2017, resigned 19 February 2018)

In addition to the attendance set out above, the ScottishPower Control and Administration Director, Head of Internal Audit and the external auditor normally attend by invitation, all meetings of the SP ACC. Other members of senior management are also invited to attend as appropriate.

## DIRECTORS' REPORT *continued*

### CORPORATE GOVERNANCE *continued*

#### ScottishPower Audit and Compliance Committee ("SP ACC") *continued*

##### Matters considered by the SP ACC during 2017

The issues that the SP ACC specifically addressed are detailed in its report which is published at: [www.scottishpower.com/pages/activities\\_report\\_of\\_the\\_audit\\_and\\_compliance\\_committee.aspx](http://www.scottishpower.com/pages/activities_report_of_the_audit_and_compliance_committee.aspx).

In addition to the issues detailed in the report above, the SP ACC in early 2018 also considered various matters which are relevant to the monitoring of the statutory audit of the Annual Report and Accounts of ScottishPower for 2017. In particular on 14 February 2018:

- the SP ACC reviewed the independence of the external auditor and submitted its conclusions on the same to the ScottishPower Board;
- as part of the SP ACC's supervision of the auditing of the financial statements, the external auditor appeared before the SP ACC to present its conclusions on the 2017 statutory audit; and
- the SP ACC reviewed the financial results to 31 December 2017 and submitted its conclusions on the same to the ScottishPower Board.

##### Significant financial statement reporting issues

In preparing the Annual Report and Accounts, there are a number of areas requiring management to apply judgement or a high degree of estimation. After discussion with management and the external auditor, the significant areas of judgement reviewed and considered by the SP ACC in relation to the 2017 Annual Report and Accounts, and how these were addressed are set out in the table below.

Significant financial judgements for the year ended 31 December 2017	How the SP ACC addressed these significant financial judgements
<b>Accounting for group and parent company pension obligations</b> The assumptions in relation to the cost to the group of providing future post-retirement benefits are set after consultation with qualified actuaries and can have a material impact on the financial position of the group. The costs, assets and liabilities of the group's defined benefit schemes are regularly reviewed. Advice is taken from independent actuaries and other specialists within the Iberdrola group on the IAS 19 valuation of the schemes including the complex assets. Further details are provided in Note 3K on page 41 and Note 18 on page 67.	The SP ACC were updated on the combined schemes' valuation and also considered the findings of the external auditor particularly in relation to the schemes' key assumptions and complexity of assets relative to current market practice. Following this review, the SP ACC supported this judgement.
<b>Recognition of Retail accrued revenue</b> Revenue from energy sales to retail customers includes estimates of the value of electricity and gas supplied between the most recent meter reading and the period end. This is based on estimates and assumptions in relation to the consumption and its valuation. Further details are provided in Note 3A on page 38 and Note 12 on page 64.	The SP ACC reviewed the estimation and valuation processes and assumptions applied in determining the recognition of accrued revenue and were updated on the impact on the financial statements. This was with particular reference to domestic electricity and gas. The SP ACC also considered the findings of the external auditor. Following this review, the SP ACC supported this judgement.
<b>Provision of Retail receivables</b> The recoverability of the group's billed energy receivables in the Retail business function is a key judgement area given the risk of customer default. The level of the group's aged debt is monitored with the provision for impairment of doubtful debts being based on assumptions derived from estimated future cash flows, the ageing profile of the debt, prior experience and an assessment of the current economic environment. Further details are provided in Note 3G.1 on page 39 and Note 12 on page 64.	The SP ACC considered the assumptions impacting the provision for impairment of doubtful debt and related charges and the processes for debt collection and provisioning. The SP ACC also considered the findings of the external auditor in this area. Following this review, the SP ACC supported this judgement.
<b>Valuation of derivative financial instruments</b> The group uses derivative financial instruments within the Energy Management function. The assumptions involved in valuing and classifying such instruments involves judgement and can have a significant impact on the group's results and financial position. Further details are provided in Note 3G.3 on page 41 and Note 21 on page 73.	The SP ACC considered the impact of derivatives on the financial statements and the controls in place to support the classification and valuation of derivatives. The SP ACC also considered the findings of the external auditor particularly in relation to the key assumptions. Following this review, the SP ACC supported this judgement.

## DIRECTORS' REPORT *continued*

### CORPORATE GOVERNANCE *continued*

#### 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 SP 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 a set of Anti-Bribery and Corruption Policies and Procedures, Crime Prevention and Anti-Fraud Guidelines, and Speaking Out Guidelines in place. Together with the Code of Ethics, these Policies, Procedures and Guidelines provide mechanisms to ensure that instances of fraud, bribery, corruption or other criminal or unethical behaviour are identified, reported and investigated. The Speaking Out guidelines incorporate a confidential external reporting service operated by an independent provider. These guidelines, which are applicable to employees and suppliers of the company, cover any incident, issue, behaviour or practice which does not comply with the Code of Ethics, including fraud, bribery, theft, misuse of company resources and conflicts of interest. There is also a process in existence within ScottishPower whereby all members of staff may report any financial irregularities to the Audit and Risk Supervision Committee of Iberdrola.

#### 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, SPCH and SPREL 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.

#### External auditor

Annually, the SP ACC reviews the external auditor's audit plan and reviews and assesses the information provided by them confirming their independence and objectivity within the context of regulatory requirements and professional standards. The external auditor contributes a further independent perspective on certain aspects of the group's internal controls over financial reporting arising from their work and reports to the SP ACC if appropriate.

Following an Iberdrola group wide tendering process in 2016 in line with relevant EU legislation, KPMG LLP were appointed as the Iberdrola group auditor for 2017. During 2017 the SP ACC also approved the proposal to the ScottishPower Board on the appointment and conditions of the engagement of the new external auditor KPMG LLP.

## DIRECTORS' REPORT *continued*

### CORPORATE GOVERNANCE *continued*

#### Auditor independence

The Audit, Risk and Supervision Committee of Iberdrola, which comprises non-executive directors, is responsible for the nomination of the external auditor. This committee and the external auditor have safeguards to avoid the possibility that the auditor's 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 auditor for sound commercial and practical reasons, including confidentiality, the conduct of such work is permissible provided that all necessary internal governance has been met.

#### Iberdrola Appointments and Remuneration Committees

There is no separate Appointments or Remuneration Committee within ScottishPower. Instead, appointments and remuneration matters relevant to ScottishPower and the company are dealt with by the Iberdrola Appointments Committee ("IAC") and the Iberdrola Remuneration Committee ("IRC"). The members of the IAC are:

María Helena Antolín Raybaud (Chairperson)	External independent
Iñigo Víctor de Oriol Ibarra	Other external
Ángel Jesús Acebes Paniagua	External independent

The members of the IRC are:

Inés Macho Stadler (Chairperson)	External independent
Iñigo Víctor de Oriol Ibarra	Other external
Juan Manuel González Serna	External independent (appointed 31 March 2017)

The IAC has the power to supervise the process of selection of directors and senior managers of the Iberdrola group companies. The Diversity Policy applied by the IAC is included within the IAC's terms of reference at:

[www.iberdrola.com/wcorp/gc/prod/en\\_US/corporativos/docs/comision\\_nombramientos.pdf](http://www.iberdrola.com/wcorp/gc/prod/en_US/corporativos/docs/comision_nombramientos.pdf).

The Diversity Policy itself is published at:

[www.iberdrola.com/wcorp/gc/prod/en\\_US/corporativos/docs/director\\_candidate\\_selection\\_policy.pdf](http://www.iberdrola.com/wcorp/gc/prod/en_US/corporativos/docs/director_candidate_selection_policy.pdf).

#### Social, environmental and ethical matters

Social, environmental and ethical ("SEE") matters are included in the overall risk and control framework and in the Risk Report which is reviewed at the monthly management meetings. 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 Social Responsibility' section of the ScottishPower website at: [www.scottishpower.com](http://www.scottishpower.com).

### DIRECTORS

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

David Wark  
Marion S Venman  
Donald Wright

#### DIRECTORS' INDEMNITY

In terms of the company's Articles of Association, a qualifying indemnity provision is in force for the benefit of all the directors of the company and of associated companies and has been in force during the financial year.

## DIRECTORS' REPORT *continued*

### STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND ACCOUNTS

The directors are responsible for preparing the Annual Report and Accounts in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they are required to prepare the group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law and have elected to prepare the parent company financial statements on the same basis.

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.

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

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

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

Each of the directors in office as at the date of this Annual 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.

### Responsibility statement of the directors in respect of the Annual Report and Accounts

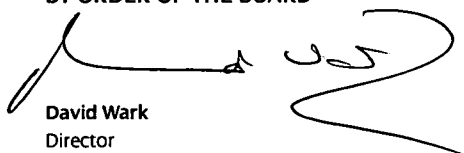
Each of the directors in office as at the date of this Annual Report and Accounts confirms that to the best of his or her knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

### AUDITOR

KPMG LLP were appointed as the auditor of the company for the period ended 31 December 2017 in place of the retiring auditor, Ernst & Young LLP.

### BY ORDER OF THE BOARD



David Wark  
Director  
27 April 2018





# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC

## 1. Our opinion is unmodified

We have audited the financial statements of Scottish Power UK plc ("the Company") for the year ended 31 December 2017 which comprise the consolidated and company balance sheets, consolidated income statement, consolidated and company statements of comprehensive income, consolidated and company statements of changes in equity, consolidated and company cash flow statements and related notes, including the accounting policies in note 3.

### In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2017 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the ScottishPower Audit and Compliance Committee ("SP ACC").

We were appointed as auditor by the directors on 11 January 2018. The period of total uninterrupted engagement is for the single financial year ended 31 December 2017. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the Financial Reporting Council ("FRC") Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

### Overview

<b>Materiality:</b> group financial statements as a whole	£28m  5.4% group profit before tax
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<b>Coverage</b>	100% of group profit before tax
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### Risks of material misstatement

<b>Recurring risks</b>	IAS 19 provision for retirement benefit obligations
	Retail accrued revenue
	Recoverability of Retail receivables
	Valuation of derivatives and hedging

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

## 2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
<b>Retirement benefit obligations</b> (Group and parent company) (£564.8 million; 2016: £442.5 million) Refer to page 19 (SP ACC statement), page 41 (accounting policy) and page 67 (financial disclosures).	<b>Subjective valuation</b> Relatively small changes in the actuarial assumptions underlying the valuation of the group's defined benefit schemes could materially impact the deficit. A significant proportion of the combined schemes' assets are more complex in nature, including investments in unlisted funds and property portfolios.	Our procedures included: <ul style="list-style-type: none"> <li>— <b>Benchmarking assumptions:</b> Challenging, with the support of our own actuarial specialists, the key assumptions applied, being the discount rate, inflation rate and mortality/life expectancy against externally derived data, including benchmarking against other schemes of a similar profile.</li> <li>— <b>Test of detail:</b> We obtained the population of scheme assets and performed substantive tests of detail on a sample to determine whether they have been appropriately valued based on information from suitably qualified and objective third parties, whose credentials we have assessed. We obtained direct confirmations from third parties, such as investment managers, to support the valuation of a sample of relevant unlisted investments and property investments.</li> <li>— <b>Assessing transparency:</b> Considering the adequacy of the group's disclosures in respect of the sensitivity of the deficit to these assumptions.</li> </ul> <b>Our results</b> <ul style="list-style-type: none"> <li>— We found the valuation of pension scheme assets and liabilities to be acceptable.</li> </ul>

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

## 2. Key audit matters: our assessment of risks of material misstatement

	The risk	Our response
<b>Recognition of Retail accrued revenues</b> (£116.6 million; 2016: £80.5 million) Refer to page 19 (SP ACC statement), page 38 (accounting policy) and page 64 (financial disclosures).	<b>Subjective valuation</b> Judgement is involved in the valuation of accrued revenue ("unbilled") which relates to estimated energy usage between customers' most recent meter reading and the period end. The estimate is based on the volume of electricity or gas expected to have been used, based on external data from the industry standard settlements system. Revenue is calculated based on these estimated volumes multiplied by a weighted average tariff price, which also carries a degree of estimation. The level of estimation is lower for customers subject to more frequent meter readings and invoicing (industrial and commercial customers).	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>— <b>Expectations vs outcomes:</b> We developed an expectation of total revenue with regards to tariff pricing information and external settlements data for energy volumes and compared to the actual total revenue recognised, including the year end accrual.</li> <li>— <b>Control observation:</b> Perform testing of the controls over pricing calculations, billing exceptions, interfaces with the general ledger and price updates.</li> <li>— <b>Historical comparison:</b> We compared the prior periods' estimates with actual volumes billed in order to assess the accuracy of estimation and challenge the validity of the current year assumption.</li> <li>— <b>Tests of detail:</b> We compared the volume data to the external settlements systems and internal billing systems.</li> <li>— <b>Our sector experience:</b> We challenged the Group's assumptions relating to volume and price used in determining the level of estimated revenue, as follows:   <i>Underlying assumption on volume</i>                Compare the estimated volume determined by the Group with benchmarks that the Group has developed based on historical experience using internal and external information around which we performed analysis, then sought and assessed explanations for variances from expected benchmarks.   <i>Underlying assumptions on price</i>                Challenge the assumptions of price per unit by comparing the price applied with current actual billing internal trends and data. Assess the overall consistency period on period of the assumptions and of the inputs to the calculation of estimated value of revenue.             </li> <li>— <b>Assessing transparency:</b> Assessing the adequacy of the group's disclosures about the degree of estimation involved in arriving at the estimated revenue.</li> </ul> <p><b>Our results</b></p> <ul style="list-style-type: none"> <li>— We found the valuation of unbilled revenue to be acceptable.</li> </ul>

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

## 2. Key audit matters: our assessment of risks of material misstatement

	The risk	Our response
<b>Provision for Retail receivables</b> (£466.5 million; 2016: £412.8 million) Refer to page 19 (SP ACC statement), page 39 (accounting policy) and page 64 (financial disclosures).	<b>Subjective valuation</b> The Retail business carries significant exposure over the recoverability of customer receivables. An allowance for doubtful debt is provided based on an estimate of future cash flows. In arriving at this estimate, management consider the current ageing profile of debt, historical collections experience and an assessment of current economic conditions.	Our procedures included: <ul style="list-style-type: none"> <li>— <b>Methodology choice:</b> To assess the appropriateness of the Company's provisioning methods, we challenged management's assumptions comparing them to historical data on cash collections and write-offs.</li> <li>— <b>Control observation:</b> Evaluate the group's controls over the Retail debt collection processes and the estimation of the bad debt provision, including the process for reconciling sales, cash receipts and the general ledger.</li> <li>— <b>Tests of detail:</b> Check whether the provision has been accurately and consistently calculated in line with group policy, test the accuracy of the ledger ageing information by verifying a sample of underlying invoicing transactions and evaluate the level of cash collected subsequent to period end.</li> <li>— <b>Assessing transparency:</b> Assess the adequacy of the group's disclosures about the degree of estimation involved in arriving at the Retail debt provision.</li> </ul> <b>Our results</b> <ul style="list-style-type: none"> <li>— We found the provision for Retail receivables to be acceptable.</li> </ul>
<b>Derivative financial instruments</b> Balances relating to hedged commodity derivatives: (current assets £46.2m; current liabilities £10.6m; non-current assets £20.5m; non-current liabilities £1.1m; 2016: current assets £48.8m; current liabilities £37.0m; non-current assets £36.7m; non-current liabilities £2.2m). Refer to page 19 (SP ACC statement), page 39 (accounting policy) and page 73 (financial disclosures).	<b>Accounting treatment</b> The group transacts in derivative instruments related to the Energy Management function which balances the supply and demand of energy commodities. These are held at fair value. Some of the derivative instruments require greater judgement in their balance sheet valuation, particularly where the life of the instrument exceeds the term of liquid market pricing information. It is therefore important that each instrument is correctly classified for valuation purposes.	Our procedures included: <ul style="list-style-type: none"> <li>— <b>Controls operation:</b> Reviewing the reconciliations between the internal trade capture systems to the external trading platforms and third party confirmations received from counterparties to ensure that trades are captured correctly within internal systems; examining the authorisation of trading transactions; and evaluating breaches of trader and/or counterparty limits to ensure that these had been investigated appropriately.</li> <li>— <b>Test of detail:</b> We obtained a breakdown of all trades which make up the income statement and mark-to-market closing balance sheet positions and performed procedures to verify the completeness of the population by selecting a sample of settlement payments to/from counterparties during the period and post period end and tracing these to underlying trades.</li> <li>— We selected a sample of trades classified as hedges and verified that the treatment adopted was appropriate in accordance with relevant standards.</li> </ul> <b>Our results</b> <ul style="list-style-type: none"> <li>— We found the accounting for derivatives to be acceptable.</li> </ul>

INDEPENDENT AUDITOR'S REPORT  
TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

3. Our application of Group materiality and an overview of the scope of our audit

Materiality for the Group financial statements as a whole was set at £28 million, determined with reference to a benchmark of Group profit before tax, normalised over the last five years due to fluctuations in the business cycle, of £581 million of which it represents 4.9%.

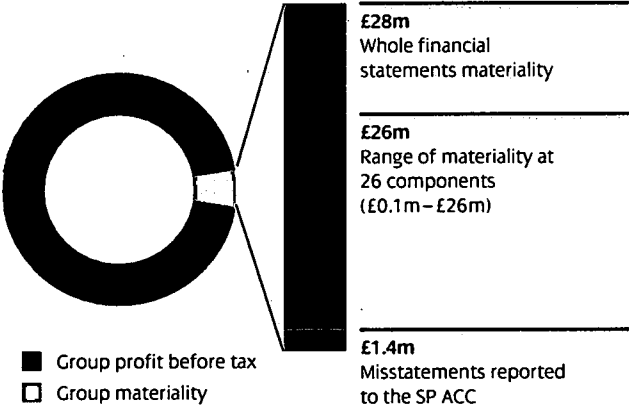
Materiality for the parent company financial statements was set with reference to total assets but capped at £26 million due to the level of Group materiality.

We agreed to report to the SP ACC any corrected or uncorrected identified misstatements exceeding £1.4 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

All of the Group's components were subject to full scope audit procedures performed in the UK by the group audit team, these components represented 100% of group revenue, profit before tax and total assets.

Group profit before tax  
£517m (2016: £674m)

Group Materiality  
£28m



# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

## 4. We have nothing to report on going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

## 5. We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

### Strategic report and directors' report

Based solely on our work on the other information:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

## 6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required 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 financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

## 7. Respective responsibilities

### Directors' responsibilities

As explained more fully in their statement set out on page 22, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

### Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities).

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH POWER UK PLC *continued*

## *Irregularities – ability to detect*

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our sector experience and through discussion with the directors and other management (as required by auditing standards), and from inspection of the company's regulatory and legal correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related company legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related financial statement items.

In addition we considered the impact of laws and regulations in the specific areas of regulatory compliance recognising the regulated nature of the company's activities. With the exception of any known or possible non-compliance, and as required by auditing standards our work in respect of these was limited to enquiry of the directors and other management and inspection of regulatory and legal correspondence.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

As with any audit, there remained a higher risk of non-detection of non-compliance with relevant laws and regulations (irregularities), as these may involve collusion, forgery, intentional omissions misrepresentations, or the override of internal controls.

## **8. The purpose of our audit work and to whom we owe our responsibilities**

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



**Philip Charles (Senior Statutory Auditor  
for and on behalf of KPMG LLP, Statutory Auditor  
Chartered Accountants**

319 St. Vincent Street  
Glasgow  
G2 5AS  
27 April 2018



# SCOTTISH POWER UK PLC AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

at 31 December 2017 and 31 December 2016

	Notes	2017 £m	2016 Restated* £m
<b>ASSETS</b>			
<b>NON-CURRENT ASSETS</b>			
Intangible assets		535.1	551.0
Goodwill	8	364.6	364.6
Other intangible assets	8	170.5	186.4
Property, plant and equipment		12,934.1	12,829.1
Property, plant and equipment in use	9	11,446.1	10,069.8
Property, plant and equipment in the course of construction	9	1,488.0	2,759.3
Financial assets		71.1	106.1
Investments in joint ventures	10	5.6	8.7
Other investments	11	1.1	1.1
Finance lease receivables	11	0.1	0.6
Derivative financial instruments	11, 21	64.3	95.7
Trade and other receivables	12	53.2	74.2
Deferred tax asset	24	–	5.2
<b>NON-CURRENT ASSETS</b>		<b>13,593.5</b>	<b>13,565.6</b>
<b>CURRENT ASSETS</b>			
Inventories	13	452.1	227.5
Trade and other receivables	12	1,477.9	1,583.4
Financial assets		107.7	206.1
Finance lease receivables	11	0.4	0.3
Derivative financial instruments	11, 21	107.3	205.8
Cash	11	45.6	35.5
<b>CURRENT ASSETS</b>		<b>2,083.3</b>	<b>2,052.5</b>
<b>TOTAL ASSETS</b>		<b>15,676.8</b>	<b>15,618.1</b>

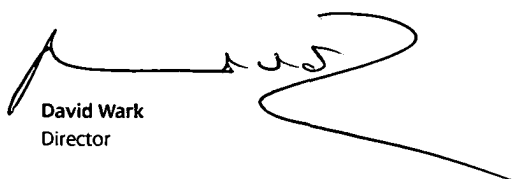


SCOTTISH POWER UK PLC AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS *continued*  
at 31 December 2017 and 31 December 2016

	Notes	2017 £m	2016 Restated* £m
<b>EQUITY AND LIABILITIES</b>			
<b>EQUITY</b>			
Of shareholders of the parent	15	5,280.5	4,014.2
Share capital	14, 15	2,192.0	872.0
Share premium	15	398.2	398.2
Hedge reserve	15	86.4	79.2
Translation reserve	15	–	0.3
Other reserves	15	14.0	14.0
Retained earnings	15	2,589.9	2,650.5
Of non-controlling interests	16	0.9	0.6
<b>TOTAL EQUITY</b>		<b>5,281.4</b>	<b>4,014.8</b>
<b>NON-CURRENT LIABILITIES</b>			
Deferred income	17	1,183.6	1,107.3
Provisions		796.6	637.4
Provisions for retirement benefit obligations	18	564.8	442.5
Other provisions	19	231.8	194.9
Bank borrowings and other financial liabilities		2,986.9	2,701.2
Loans and other borrowings	20	2,986.4	2,698.1
Derivative financial instruments	11, 21	0.5	3.1
Trade and other payables	23	33.7	35.2
Deferred tax liabilities	24	738.2	721.5
<b>NON-CURRENT LIABILITIES</b>		<b>5,739.0</b>	<b>5,202.6</b>
<b>CURRENT LIABILITIES</b>			
Provisions	19	360.9	311.5
Bank borrowings and other financial liabilities		2,750.3	4,346.4
Loans and other borrowings	20	2,681.4	4,184.9
Derivative financial instruments	11, 21	68.9	161.5
Trade and other payables	23	1,514.9	1,714.5
Current tax liabilities		30.3	28.3
<b>CURRENT LIABILITIES</b>		<b>4,656.4</b>	<b>6,400.7</b>
<b>TOTAL LIABILITIES</b>		<b>10,395.4</b>	<b>11,603.3</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>15,676.8</b>	<b>15,618.1</b>

\* Comparative figures have been restated (refer to Note 2).

Authorised for issue by the Board and signed on its behalf on 27 April 2018 by:

  
David Wark  
Director

The accompanying Notes 1 to 37 are an integral part of the consolidated balance sheets at 31 December 2017 and 31 December 2016.

# SCOTTISH POWER UK PLC AND SUBSIDIARIES

## CONSOLIDATED INCOME STATEMENTS

for the years ended 31 December 2017 and 31 December 2016

	Notes	2017 £m	2016 Restated* £m
Revenue		5,239.1	5,142.6
Procurements		(3,113.8)	(2,915.9)
<b>GROSS MARGIN</b>		<b>2,125.3</b>	<b>2,226.7</b>
<b>NET OPERATING EXPENSES</b>		<b>(677.3)</b>	<b>(645.7)</b>
Net personnel expenses	25	(286.5)	(262.5)
Staff costs	25	(429.1)	(395.1)
Capitalised staff costs	25	142.6	132.6
Net external services		(390.8)	(383.2)
External services		(517.2)	(520.5)
Other operating income		126.4	137.3
Taxes other than income tax	26	(223.3)	(193.2)
<b>GROSS OPERATING PROFIT</b>		<b>1,224.7</b>	<b>1,387.8</b>
Depreciation and amortisation charge, allowances and provisions	27	(570.9)	(556.5)
<b>OPERATING PROFIT</b>		<b>653.8</b>	<b>831.3</b>
Result of companies accounted for using the equity method	10	0.9	0.9
Gains on disposal of non-current assets		0.5	1.6
Losses on disposal of non-current assets		(0.1)	-
Gain on disposal of subsidiaries	36	20.2	-
Finance income	28	15.4	24.2
Finance costs	29	(174.2)	(184.3)
<b>PROFIT BEFORE TAX</b>		<b>516.5</b>	<b>673.7</b>
Income tax	30	(90.4)	(92.7)
<b>NET PROFIT FOR THE YEAR</b>		<b>426.1</b>	<b>581.0</b>
Non-controlling interests	16	(0.2)	(0.1)
<b>NET PROFIT FOR THE YEAR ATTRIBUTABLE TO THE PARENT</b>		<b>425.9</b>	<b>580.9</b>

\* Comparative figures have been restated (refer to Note 2).

All results relate to continuing operations, other than the French and German operations (refer to Note 36).

The accompanying Notes 1 to 37 are an integral part of the consolidated income statements for the years ended 31 December 2017 and 31 December 2016.

SCOTTISH POWER UK PLC AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
for the years ended 31 December 2017 and 31 December 2016

	Note	2017 £m	2016 £m
<b>NET PROFIT FOR THE YEAR</b>		<b>426.1</b>	<b>581.0</b>
<b>OTHER COMPREHENSIVE INCOME</b>			
Items that may be subsequently reclassified to the income statement:			
Cash flow hedges:			
Change in the value of cash flow hedges	15	27.9	79.8
Tax relating to cash flow hedges	15	(5.3)	(15.0)
		<b>22.6</b>	<b>64.8</b>
Items that will not be reclassified to the income statement:			
Actuarial losses on retirement benefits:			
Actuarial losses on retirement benefits	15	(222.9)	(251.4)
Tax relating to actuarial losses on retirement benefits	15	36.4	42.1
Cash flow hedges:			
Change in the value of cash flow hedges	15	(19.0)	78.8
Tax relating to cash flow hedges	15	3.6	(15.7)
		<b>(201.9)</b>	<b>(146.2)</b>
<b>OTHER COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>(179.3)</b>	<b>(81.4)</b>
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>246.8</b>	<b>499.6</b>
Total comprehensive income for the year attributable to equity holder of the parent		246.6	499.5
Total comprehensive income for the year attributable to non-controlling interests		0.2	0.1
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>246.8</b>	<b>499.6</b>

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY  
for the years ended 31 December 2017 and 31 December 2016

	Attributable to equity holder of the parent							Non-controlling interests £m	Total equity £m
	Share capital £m	Share premium £m	Hedge reserve £m	Translation reserve £m	Other reserves £m	Retained earnings £m	Total £m		
At 1 January 2016	872.0	398.2	(48.7)	(0.6)	14.0	2,941.9	4,176.8	0.5	4,177.3
Total comprehensive income for the year	-	-	127.9	-	-	371.6	499.5	0.1	499.6
Exchange movement on translation of overseas results and net assets	-	-	-	0.9	-	-	0.9	-	0.9
Dividends	-	-	-	-	-	(663.0)	(663.0)	-	(663.0)
At 1 January 2017	872.0	398.2	79.2	0.3	14.0	2,650.5	4,014.2	0.6	4,014.8
Total comprehensive income for the year	-	-	7.2	-	-	239.4	246.6	0.2	246.8
Exchange movement on translation of overseas results and net assets	-	-	-	0.2	-	-	0.2	-	0.2
Group restructuring	-	-	-	(0.5)	-	-	(0.5)	0.1	(0.4)
Share capital issued (refer to Note 14)	1,320.0	-	-	-	-	-	1,320.0	-	1,320.0
Dividends	-	-	-	-	-	(300.0)	(300.0)	-	(300.0)
<b>At 31 December 2017</b>	<b>2,192.0</b>	<b>398.2</b>	<b>86.4</b>	<b>-</b>	<b>14.0</b>	<b>2,589.9</b>	<b>5,280.5</b>	<b>0.9</b>	<b>5,281.4</b>

The accompanying Notes 1 to 37 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 2017 and 31 December 2016.

SCOTTISH POWER UK PLC AND SUBSIDIARIES  
CONSOLIDATED CASH FLOW STATEMENTS  
for the years ended 31 December 2017 and 31 December 2016

	2017 £m	2016 Restated* £m
<b>Cash flows from operating activities</b>		
Profit before tax	516.5	673.7
Adjustments for:		
Depreciation, amortisation and impairment	498.3	489.0
Research and development expenditure credit	—	(0.8)
Change in provisions	423.0	353.5
Result of companies accounted for using the equity method	(0.9)	(0.9)
Capital grants and transfer of assets from customers	(35.3)	(32.3)
Finance income and costs	158.8	160.1
Net losses on disposal/write-off non-current assets	3.8	0.7
Gain on disposal of subsidiaries	(20.2)	—
Movement in retirement benefits	(110.0)	(80.1)
Net fair value losses/(gains) on operating derivatives	23.9	(54.1)
Movement in deferred income	(0.1)	(0.1)
Movement in plant maintenance stocks	(0.7)	(7.9)
Changes in working capital:		
Change in trade and other receivables	(35.0)	(15.8)
Change in inventories	(586.1)	(232.0)
Change in trade and other payables	60.8	87.5
Provisions paid	(9.8)	(17.5)
Assets received from customers (cash contributions)	107.3	126.7
Income taxes paid	(37.5)	(107.9)
Interest received	10.3	14.3
Dividends received	0.1	0.1
<b>Net cash flows from operating activities (i)</b>	<b>967.2</b>	<b>1,356.2</b>
<b>Cash flows from investing activities</b>		
Investments in intangible assets	(44.5)	(43.3)
Investments in property, plant and equipment (net of capital grants)	(1,569.9)	(1,569.0)
Disposal of jointly controlled entities	4.0	23.3
Proceeds from disposal of property, plant and equipment	33.4	2.2
Net proceeds received from disposal of subsidiary	21.8	—
Cash disposed	(1.5)	—
Decrease in amounts due from Iberdrola group companies – current loans receivable	112.0	89.0
<b>Net cash flows from investing activities (ii)</b>	<b>(1,444.7)</b>	<b>(1,497.8)</b>
<b>Cash flows from financing activities</b>		
(Decrease)/increase in amounts due to Iberdrola group companies – current loans payable	(1,147.3)	634.4
Increase in amounts due to Iberdrola group companies – non-current loans payable	989.7	330.6
Cash inflows from borrowings	1.1	22.4
Share capital issued	1,320.0	—
Dividends paid to company's equity holder	(300.0)	(663.0)
Interest paid	(169.7)	(171.2)
Repayments of borrowing	(206.3)	—
<b>Net cash flows from financing activities (iii)</b>	<b>487.5</b>	<b>153.2</b>
<b>Net increase in cash and cash equivalents (i)+(ii)+(iii)</b>	<b>10.0</b>	<b>11.6</b>
<b>Effect of foreign exchange rates on cash and cash equivalents</b>	<b>—</b>	<b>0.2</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>35.5</b>	<b>23.7</b>
<b>Cash and cash equivalents at end of year</b>	<b>45.5</b>	<b>35.5</b>
Cash and cash equivalents at end of year comprises:		
Cash	45.6	35.5
Bank overdraft	(0.1)	—
<b>Cash flow statement cash and cash equivalents</b>	<b>45.5</b>	<b>35.5</b>

\* Comparative figures have been restated (refer to Note 2).

The accompanying Notes 1 to 37 are an integral part of the consolidated cash flow statements for the years ended 31 December 2017 and 31 December 2016.

# NOTES TO THE CONSOLIDATED ACCOUNTS

31 December 2017

## 1 GROUP ACTIVITIES

### A. COMPANY INFORMATION

#### Scottish Power UK plc

The group's holding company is Scottish Power UK plc (registered company number SC117120), a private company limited by shares. It is incorporated in Scotland and its registered address is 320 St. Vincent Street, Glasgow, G2 5AD.

### B. GROUP INFORMATION

The group provides electricity transmission and distribution services in the UK, supplies gas and electricity services to homes and businesses across the UK, operates electricity generation and gas storage facilities and provides associated energy management activities in the UK. It also conducts renewable energy activities across the UK and Republic of Ireland, and until 1 August 2017, in France and Germany.

As described in Note 6, in line with IFRS 8 'Operating Segments' ("IFRS 8"), the group defines operating segments based on a combination of factors, principally differences in products and services and the regulatory environment in which the business operates. The group reported three segments during the year: Energy Networks, Energy Wholesale and Retail, and Renewables.

#### Energy Networks

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

#### Energy Wholesale and Retail

The generation of electricity from the group's own power stations, the purchase of external supplies of coal (until 24 March 2016) and gas for the generation of electricity, the purchase of external supplies of electricity and gas for onward sale to customers and the optimisation of gas storage. The business is also involved in the sale of electricity to market participants in the UK and the sale of electricity and gas to industrial and domestic customers, together with related billing and collection activities.

#### Renewables

The construction and the development of renewable energy generation assets and the generation and sale of electricity and Renewables Obligation Certificates ("ROCs") from those 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 ("IFRS") and International Financial 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 2017. Both the group and company Accounts are prepared in accordance with the Accounting Policies set out in Note 3.

### A1. CHANGES IN PRESENTATION

#### A1.1 ROCs and LECs

The accounting for ROCs and Levy Exemption Certificates ("LECs") has been aligned to that of carbon emissions allowances due to the similar nature of these transactions (refer to Note 3.1). Therefore the associated assets and liabilities on the balance sheet are no longer presented net within Trade payables and receivables, but the obligation provision and purchased certificates are presented gross within Provisions and Inventories respectively. The prior period figures have been adjusted accordingly. There is no impact on the income statement or net assets. The impact on the balance sheet was to increase Inventories by £143.4 million, increase Provisions by £260.0 million, increase Trade and other receivables by £99.4 million and decrease Trade and other payables by £17.2 million.

#### A1.2 CERTAIN HEDGE TRADES

Following a review of non-speculative wholesale market trades, these are now accounted for net such that revenue reflects only the retail delivery of gas and electricity to the group's domestic and non-domestic customers, and any net delivery of the generation output of the Energy Wholesale business function to the market. Procurements reflects only the net purchase of electricity and gas for onward sale to retail customers and the net purchase of gas for the generation of electricity. Previously, net sales and purchases during certain market windows in which the group is required under regulations to stand ready to sell or buy, were presented in Revenue and all other non-speculative trades were shown gross in Revenue and Procurements. The effect of this has been to decrease each of the prior year's Revenue and Procurements by £279.9 million. This had no effect on profit for the prior year or on the balance sheet.

#### A1.3 CASH FLOW PRESENTATION

The group participates in arrangements whereby subsidiaries' primary source of short-term funding for cash management purposes is from intercompany loans drawn down from other group undertakings. Similarly, subsidiaries with surplus cash, lend this to other group undertakings for the purposes of their cash management. The short-term loans are repayable on demand. On the balance sheet, these funds are recorded within current loans and borrowings and current trade and other receivables respectively. In prior years, the group and company reported these funds within cash and cash equivalents for the purposes of the cash flow statement. During the year, the directors have reviewed the treatment of these funds and concluded that funds recorded within current loans and borrowings should be recorded within financing cash flows and funds recorded within current trade and other receivables should be recorded within investing cash flows for the purposes of the cash flow statement. The directors have also concluded that for the company, funds recorded within non-current trade and other receivables should be recorded within investing cash flows. The 2016 cash flow statements for the group and the company have therefore been adjusted. For the group, the effect on the prior year is to increase the net cash flows from financing activities by £634.5 million, increase the net cash flows from investing activities by £89.0 million and increase the cash and cash equivalents reported for the purpose of the cash flow statement by £3,241.8 million. For the company, the effect on the prior year is to increase the net cash flows from financing activities by £108.2 million, decrease the net cash flows from investing activities by £71.9 million and increase the cash and cash equivalents reported for the purpose of the cash flow statement by £1,157.4 million. These restatements had no impact on net assets, equity, the statements of comprehensive income or the balance sheets.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 2 BASIS OF PREPARATION *continued*

### A. BASIS OF PREPARATION OF THE ACCOUNTS *continued*

#### A2. CHANGE IN ACCOUNTING ESTIMATE

##### A2.1 CHANGE IN USEFUL LIFE OF CCGTS

During 2017, Iberdrola performed a review of the life of their CCGT stations; the analysis reviewed both internal and external sources of information. As a result of this review, the group has increased the useful life of CCGT stations to 40 years compared to the 35 years previously applied. This change in estimate has been applied prospectively from 1 January 2017. The impact of this change has been to reduce the depreciation charge of the group for the current year by £8.0 million. It is impracticable to estimate the effect of this change on future periods.

### B. ACCOUNTING STANDARDS

In preparing these Accounts, the group has applied all relevant IAS, IFRS and IFRIC Interpretations that have been adopted by the EU as of the date of approval of these Accounts and that are mandatory for the financial year ended 31 December 2017.

For the year ended 31 December 2017, the group has applied the following amendments for the first time:

Standard	Notes
• Amendments to IAS 12 'Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses'	(a)
• Amendments to IAS 7 'Statement of Cash Flows: Disclosure Initiative'	(a)
• Annual improvements to IFRS Standards 2014-2016 Cycle	(a), (b)

(a) The application of these pronouncements has not had a material impact on the group's accounting policies, financial position or performance.

(b) This pronouncement includes amendments to three standards. The amendments to IFRS 12 'Disclosure of Interests in Other Entities' have been applied by the group effective 1 January 2017. Refer to footnote (d) below for details of other amendments in the pronouncement.

The following new standards and amendments to standards have been issued by the International Accounting Standards Board ("IASB") but have an effective date after the date of these financial statements or have not been endorsed by the EU, thus have not been implemented by the group:

Standard	Notes	IASB effective date (for periods commencing on or after)	Planned date of application by the group
• Annual Improvements to IFRS Standards 2014 – 2016 Cycle	(c), (d)	1 January 2018	1 January 2018
• IFRS 9 'Financial Instruments'	(e)	1 January 2018	1 January 2018
• IFRS 15 'Revenue from Contracts with Customers' (including 'Amendments to IFRS 15: Effective date of IFRS 15' and 'Clarifications to IFRS 15 Revenue from Contracts with Customers')	(f)	1 January 2018	1 January 2018
• Amendments to IAS 40 'Investment Property: Transfers of Investment Property'	(c)	1 January 2018	1 January 2018
• Amendments to IFRS 2 'Share-based Payment: Clarification and Measurement of Share-based Payment Transactions'	(c)	1 January 2018	1 January 2018
• Amendments to IFRS 4 'Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts'	(c)	1 January 2018	1 January 2018
• IFRIC 22 'Foreign Currency Transactions and Advance Consideration'	(c)	1 January 2018	1 January 2018
• IFRS 16 'Leases'	(h)	1 January 2019	1 January 2019
• IFRIC 23 'Uncertainty over Income Tax Treatments'	(c), (g)	1 January 2019	1 January 2019
• Amendments to IFRS 9 'Financial Instruments: Prepayment Features with Negative Compensation'	(c)	1 January 2019	1 January 2019
• Amendments to IAS 28 'Investments in Associates and Joint Ventures: Long-term Interests in Associates and Joint Ventures'	(c), (g)	1 January 2019	1 January 2019
• Annual Improvements to IFRS Standards 2015-2017 Cycle	(c), (g)	1 January 2019	1 January 2019
• Amendments to IAS 19 'Employee Benefits: Plan Amendment, Curtailment or Settlement'	(c), (g)	1 January 2019	1 January 2019
• IFRS 17 'Insurance Contracts'	(c), (g)	1 January 2021	1 January 2021
• IFRS 14 'Regulatory Deferral Accounts'	(c), (g), (i)	1 January 2016	To be decided
• Amendments to IFRS 10 'Consolidated Financial Statements' and IAS 28 'Investments in Associates and Joint Ventures': 'Sale or Contribution Assets between an Investor and its Associate or Joint Venture'	(c), (g), (j)	Deferred indefinitely	To be decided

(c) The future application of this pronouncement is not expected to have a material impact on the group's accounting policies, financial position or performance.

(d) This pronouncement includes amendments to three standards. The amendments to IFRS 1 'First-time Adoption of International Financial Reporting Standards' and IAS 28 'Investments in Associates and Joint Ventures' have an effective date of 1 January 2018. The amendments to IFRS 12 'Disclosure of Interests in Other Entities' have an effective date of 1 January 2017 (refer to footnote (b) above).

(e) IFRS 9 'Financial Instruments' is effective for the group as from 1 January 2018. The group considers that the new classification and measurement criteria will not have a material impact on the group's equity as at 1 January 2018. Most financial assets will continue to be valued at amortised cost, except for equity instruments and derivative financial instruments which will continue to be recorded at fair value.

The group will apply the general model for the recognition of expected credit losses to all financial assets, except for trade receivables and leases, to which the simplified model will be applied. Given the high credit quality of the financial assets, the expected credit loss adjustment is only £1.4 million for the group (£2.2 million for the company).

IFRS 9 enables more economic hedging instruments and hedged items to qualify for hedge accounting than currently under IAS 39 'Financial Instruments: Recognition and Measurement' ("IAS 39"); principally the hedging of risk components in non-financial contracts and the consideration as a hedged item of a combination of a derivative and an item which could meet the characteristics of a hedged item. On implementation at 1 January 2018, this will not have a material impact on the group's equity.

In the current and previous years' accounts, the group has applied the criteria set out in Note 3G for those cases where there are no material changes to financial liabilities.

(f) IFRS 15 'Revenue from Contracts with Customers' and the associated amendments and clarifications are effective for the group as from 1 January 2018. The group considers that the application of IFRS 15 will not have a material impact on the group's financial position or performance but will continue to refine its accounting policies and monitor emerging industry practice in relation to this standard. The one exception is the effect of capitalising the incremental costs of obtaining certain customer contracts. The group will transition to IFRS 15 using the modified retrospective approach; which will require any cumulative impact of applying this standard to be recognised on implementation at 1 January 2018. The impact of the customer capture costs will be to record a new asset class on the consolidated balance sheet of £50.1 million as at 1 January 2018 with a corresponding increase in equity. The asset will be amortised on a straight-line basis over the average customer retention period. No modifications are required to the group's IT systems or processes as a result of this standard.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 2 BASIS OF PREPARATION *continued*

#### B. ACCOUNTING STANDARDS *continued*

(g) This pronouncement has not yet been endorsed by the EU.

(h) The group is currently analysing the impact of implementing IFRS 16 'Leases' which is effective for the group as from 1 January 2019. The group's principal leases relate to land for wind farms and sub-stations, property and vehicles. Most of these leases are classified as operating leases under IAS 17 'Leases'. The group expects to recognise 'right-of-use' assets and corresponding lease liabilities where the group is a lessee; the value of which is expected to be greater than the future minimum lease payments disclosed in Note 9(c). The group has tentatively decided to take the exemptions offered by IFRS 16 to exclude short-term leases and leases of low value assets from the recognition requirements in the standard. Leases of intangible assets will be considered for inclusion within the scope of IFRS 16 based on the nature of the underlying asset. The group will quantify the expected impact of the implementation of IFRS 16 based on the different transition options available at the date of its first application. The group is currently modifying its IT systems in order to adapt to the new requirements. This analysis will continue during 2018.

(i) The endorsement process of this interim standard has not been launched as the EU has decided to wait for the final standard to be issued.

(j) The IASB set the effective date of this pronouncement as for periods commencing on or after 1 January 2016. However, in December 2015, the IASB postponed the effective date indefinitely pending the outcome of its research project on the equity method of accounting. The EU endorsement process for this pronouncement has been postponed, awaiting a revised exposure draft from the IASB. The effective date will be amended in due course.

The Energy Companies Obligation ("ECO") was established on 4 December 2012 by The Electricity and Gas (Energy Company Obligation) Order 2012 ("the Order"). It imposes a legal obligation on larger energy suppliers to deliver energy efficiency measures to domestic energy users.

Once a supplier has been considered eligible for the ECO obligation, based on their domestic customer numbers, the amount of the obligation is established based on the amount of energy supplied to such domestic customers. The overall obligation period is multiannual and the obligation period is broken down into different phases. For each phase, Ofgem determines the amount of each supplier's obligation based on the domestic energy supplied by each energy supplier as a proportion of the total domestic energy supplied by all suppliers during the relevant notification period.

The ECO obligation commenced on 1 January 2013 and was initially expected to run to 31 March 2015. On 5 December 2013 the UK Government announced an extension of the overall obligation period from 31 March 2015 to 31 March 2017. The scheme was subsequently extended further to cover the period from 1 April 2017 to 30 September 2018.

The UK Government have announced that ECO will be replaced with new longer term supplier obligation to reduce carbon emissions and focus on the fuel poor. The UK Government launched a consultation on this new obligation on 30 March 2018.

The group considers that the appropriate accounting treatment is prescribed by IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' ("IAS 37"), as this obligation complies with the three features to be considered for a provision (present obligation, probable outflow of resources and a reliable estimate can be made). In accordance with a legal opinion obtained by the group, it is considered that an obligation arises for each phase of the overall obligation period. For this reason, it is appropriate to consider this obligation as an additional cost of supply to domestic customers, as this activity constitutes the obligating event, as defined under IAS 37.

The FRC staff paper 'Accounting for the Energy Company Obligation', dated 27 September 2013, indicates that the expenditure should be recognised as the assigned measures are being implemented, regardless of the rate at which energy is supplied to the domestic customers. The external auditor has determined that this is the only accounting treatment which is acceptable.

Based on the FRC staff paper and the opinion of the external auditor, the group has recorded the expense in its financial statements as the measures were actually implemented during the year. This accounting treatment involves recording £3.4 million (2016 £5.2 million) in addition to the amount that would have resulted from following a recognition rate of the obligation consistent with the rate of energy supplied to domestic customers during the accounting period.

#### C. BASIS OF CONSOLIDATION

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

Subsidiaries are those entities which the group has the right to control, generally where a shareholding 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. If the fair value of the net assets acquired is in excess of the cost of acquisition, the group reassesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed, and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the reassessment still results in an excess of the fair value of the net assets acquired over the cost of acquisition, then the gain is recognised in profit or loss.

The interest of non-controlling shareholders is initially stated at the non-controlling party's proportion of the fair values of the assets and liabilities recognised. In a business combination achieved in stages, the previously held equity interest in the acquiree is remeasured at its acquisition date fair value and resulting gain or loss recognised in profit or loss.

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 the 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 2017

### 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 "company" 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 (EXCLUDING EMISSIONS ALLOWANCES, ROCs AND LECs)
- I. EMISSIONS ALLOWANCES, ROCs AND LECs
- J. GRANTS AND TRANSFERS OF ASSETS FROM CUSTOMERS
- K. RETIREMENT BENEFITS
- L. DECOMMISSIONING COSTS
- M. FOREIGN CURRENCIES
- N. TAXATION
- O. 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 customers for use of the distribution network, which are set by price controls which determine the amount of allowed revenue. Distribution revenue includes accruals in respect of unbilled income relating to units transferred over the network.

**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 sold during the year.

**Wholesale** – revenue comprises the 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.



## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 3 ACCOUNTING POLICIES *continued*

#### C. INTANGIBLE ASSETS (EXCLUDING GOODWILL)

For both the group and the company, 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 seven years.

#### D. PROPERTY, PLANT AND EQUIPMENT

The group and company property, plant and equipment is stated at cost and is generally depreciated on a straight-line basis over the estimated operational lives of the assets. Property, plant and equipment includes capitalised employee costs, 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 of the estimated remaining lives and residual values of property, plant and equipment are undertaken annually. 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	4-105
Fossil fuel plants	2-46
Combined cycle gas turbines	2-40
Gas storage facilities	10-35
Wind farms	24-40
Transmission facilities	40
Distribution facilities	24-40
Meters and measuring devices	6-10
Other facilities and other items of property, plant and equipment	2-50

#### 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(s) or the arrangement conveys a right to use the asset(s), 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 and company classify 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 and the company review the carrying amount of their 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 ("CGU") to which the asset belongs.

#### 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 a provision 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.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 3 ACCOUNTING POLICIES *continued*

#### G. FINANCIAL INSTRUMENTS *continued*

##### G1. ACCOUNTING POLICIES UNDER IAS 39 *continued*

- (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.
- (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 below).
- (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 (until 24 March 2016) 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, 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 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 2017

### 3 ACCOUNTING POLICIES *continued*

#### G. FINANCIAL INSTRUMENTS *continued*

##### G3. HEDGE ACCOUNTING *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 are 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 (EXCLUDING EMISSIONS ALLOWANCES, ROCs AND LECs)

Inventories are valued at the lower of cost and net realisable value. Cost includes all directly attributable costs incurred in bringing the inventories to their present location and condition.

#### I. EMISSIONS ALLOWANCES, ROCs AND LECs

The group participates in the EU ETS and the Renewables Obligation ("RO") scheme administered by Ofgem. As there are no specific rules under IFRS dealing with the treatment of emissions allowances or ROCs and LECs, the group, in alignment with Iberdrola group accounting policy, classifies purchased emissions allowances and ROCs and LECs as inventories as they are consumed in the production process. Such allowances and certificates are recognised at their acquisition cost and are charged to the income statement as the obligations arise. Internally generated ROCs are awarded by Ofgem from own generation and are measured at market price.

The group recognises liabilities in respect of its obligations to deliver both schemes at the value at which these allowances and certificates were initially recorded on the balance sheet. Any estimated shortfall in the liabilities are calculated based on the market price of the allowances and relevant buyout price and estimated recycle price at the balance sheet date respectively.

#### J. GRANTS AND TRANSFERS OF ASSETS FROM CUSTOMERS

Capital and revenue grants and transfers of assets from customers are initially credited to Deferred income.

Capital grants are released to the income statement in equal instalments over the estimated operational lives of the related assets. Revenue grants are released to the income statement over the period in which they are intended to contribute to expenditure incurred.

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 in equal instalments over the estimated operational lives of the related assets.

#### K. RETIREMENT BENEFITS

The group provides two defined benefit schemes and one defined contribution retirement scheme in the UK.

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. Remeasurements of the net defined benefit liability are recognised, 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. Net interest on the net defined benefit liability or asset is included within Finance costs and Finance income, 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.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 3 ACCOUNTING POLICIES *continued*

#### L. 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.

#### M. 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.

The results and cash flows of overseas subsidiaries are translated to Sterling at average rates of exchange. The net assets of any such subsidiaries, including fair value adjustments and the goodwill arising on their acquisition, are translated to Sterling at the closing rates of exchange ruling at the balance sheet date.

#### N. TAXATION

The group's and the company's assets and liabilities for current tax are calculated using the tax rates that have been enacted or substantively enacted at 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.

#### O. 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 arise directly from its operations. The group also holds other investments, finance lease receivables and enters into derivative contracts.

During the year ended 31 December 2017, 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. Details of the governance structure in place are summarised below.

During the year under review, the ScottishPower governance structure and so that of the group, was supported by risk policies approved by the ScottishPower Board together with relevant risk guidelines that were approved by the ScottishPower Board. These risk policies are adopted and the risk limits and indicators within the guidelines were subsequently approved by the Boards of the group's businesses. ScottishPower's 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 business 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.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 4 FINANCIAL RISK MANAGEMENT POLICY *continued*

The position on risk and strategy for risk management were contained in the Risk Policy for Iberdrola's businesses in the UK (i.e. ScottishPower). The ScottishPower Board adopted 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 ensures 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.

A clear reporting structure was implemented within the group. It ensures that the portfolios were 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, credit watch, credit exposure, accounting and insurance reports.

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

#### (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. 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.

The Risk Management function employs additional techniques such as VaR, to assist in measuring risk within the volume exposure by tenor limits. 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, which utilises historical energy market forward price curve changes to estimate the potential unfavourable impact of price changes in the portfolio positions. The quantification of market risk using VaR provides a consistent measure of risk and sensitivity across the group's continually changing portfolio, however, 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 application of the VaR methodology has evolved to include the total forecasted volumes for the generation assets and retail contracts to provide a more accurate measure of the risk associated with the volume exposure by tenor limits. The group's VaR measures are shown in the table below:

	2017 £m	2016 £m
VaR	28.5	42.0
Average VaR over prior year	31.1	29.0
Maximum VaR over prior year	46.6	42.0
Minimum VaR over prior year	16.3	18.5

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 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.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 4 FINANCIAL RISK MANAGEMENT POLICY *continued*

#### (a) Energy market risk *continued*

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. Coal hedging ceased during 2016 following the closure of Longannet.

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 the existing level of and predicted changes in customer numbers and historic profiles of demand, plus the existing level of and predicted changes in generating activity, all of which are highly probable of occurring. The associated cash flows extend until 2021 for electricity, 2020 for gas and 2019 for 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.

Aggregate portfolio risk is monitored and reported by a Credit Value-at-Risk 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 2017 and 2016, 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:

	2017 £m	2016 £m
<b>Past due but not impaired:</b>		
Less than 3 months	110.3	98.3
Between 3 and 6 months	26.7	36.6
Between 6 and 12 months	37.1	38.8
After more than 12 months	20.4	14.0
	<b>194.5</b>	<b>187.7</b>

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 a provision for impairment.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 4 FINANCIAL RISK MANAGEMENT POLICY *continued*

### (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 Iberdrola's. The group's financing structure is determined by its position in the wider Iberdrola group. The company holds investment grade ratings with Moody's Investor Services (Baa1), Standard & Poor's Rating Services (BBB+) and Fitch Ratings (BBB+).

### (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 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 company.

The tables below summarise the maturity profile of the group's financial liabilities as at 31 December 2017 and 31 December 2016 based on contractual undiscounted payments.

#### Financial liabilities (excluding commodity derivatives)

	2017						Total £m
	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	2023 and thereafter £m	
Cash outflows							
Derivative financial instruments (excluding commodity derivatives)*	138.6	0.3	0.1	–	–	–	139.0
Loans and other borrowings	2,867.5	299.3	144.0	435.4	117.5	3,071.6	6,935.3
Payables**	1,212.2	2.1	1.0	0.8	0.6	–	1,216.7
	4,218.3	301.7	145.1	436.2	118.1	3,071.6	8,291.0
	2016 Restated ***						Total £m
	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 and thereafter £m	
Cash outflows							
Derivative financial instruments (excluding commodity derivatives)*	107.5	30.6	1.1	–	–	–	139.2
Loans and other borrowings	4,615.4	286.9	275.5	229.0	408.9	2,164.6	7,980.3
Payables**	1,382.1	2.9	1.7	–	–	–	1,386.7
	6,105.0	320.4	278.3	229.0	408.9	2,164.6	9,506.2

\* The above liquidity analysis is stated after the impact of counterparty netting (refer to Note 11 (c)).

\*\* Contractual cash flows exclude accrued interest as these cash flows are included within loans and other borrowings.

\*\*\* Comparatives have been restated (refer to Note 2).

### 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').

	2017						Total £m
	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	2023 and thereafter £m	
Net cash outflows	191.8	140.9	38.9	4.5	–	–	376.1
	2016						Total £m
	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 and thereafter £m	
Net cash outflows	130.0	88.5	39.7	0.9	–	–	259.1

Details of the group's contractual commitments are given in Note 33.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 4 FINANCIAL RISK MANAGEMENT POLICY *continued*

### (c) Treasury risk *continued*

#### (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

	2017 £m	2016 £m
Fixed rate	2,541.3	2,019.0
Variable rate	3,126.5	4,864.0
	5,667.8	6,883.0

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 Retail Prices Index ("RPI").

The variable rate debt consists of a £93.8 million (2016 £104.6 million) Japanese Yen ("JPY") loan, £283.3 million (2016 £273.6 million) inflation linked bonds, £194.0 million (2016 £200.3 million) LIBOR debt, £85.4 million (2016 £439.5 million) EURIBOR debt and £2,470.0 million (2016 £3,846.0 million) loans linked to Base.

The interest on the £93.8 million 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 on this debt.

For the inflation linked bonds, if RPI was to increase by 1% the impact on the annual interest rate charge would be £0.3 million. If RPI was to increase by 1% the impact on the capital would be £2.8 million.

For LIBOR/EURIBOR linked debt excluding the JPY debt, a 1% increase in the rate would result in a £2.8 million increase in the full year interest charge.

The interest rate on the short-term variable rate debt is linked to Base, a 1% increase in the Base rate would result in £24.7 million increase in the full year interest charge.

#### 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 assets 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 required hedging criteria.

#### Fair value hedges

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.

Hedging the value of currency denominated intercompany loans: the group has provided funding to other Iberdrola companies denominated in currencies other than Sterling. The value of the group's asset with respect to those loans is subject to foreign exchange risk and interest rate risk. As a result the group has entered into cross currency swaps and has designated those within a fair value hedging relationship where they meet the required hedging criteria.

#### 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.



## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 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. The group has no such policies. In preparing the consolidated Accounts in conformity with IFRS, the group 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 (a) to (e) 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) 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. 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 21 respectively.

At 31 December 2017, the carrying value of derivative financial assets was £171.6 million (2016 £301.5 million) and the carrying value of derivative financial liabilities was £69.4 million (2016 £164.6 million).

#### (b) RETAIL 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 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 billed and unbilled revenue is estimated and recorded in Revenue.

Billed revenue, for which payment has not yet been received, is included in Trade receivables and unbilled revenue is included within Accrued income in the consolidated balance sheet. Billed revenue relating to the group's retail customers included within the consolidated balance sheet at 31 December 2017 amounted to £466.5 million (2016 £412.8 million). Unbilled revenue relating to the group's retail customers included within the consolidated balance sheet at 31 December 2017 amounted to £116.6 million (2016 £80.5 million).

#### (c) IMPAIRMENT OF TRADE RECEIVABLES

Trade receivables are stated net of a provision 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 2017 amounted to £125.8 million (2016 £120.5 million) and trade receivables and accrued income (net of the provision for impairment) amounted to £810.7 million (2016 £806.5 million as restated).

#### (d) IMPAIRMENT OF GOODWILL

Goodwill is reviewed for impairment at least annually. 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 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 2017, the carrying value of goodwill amounted to £364.6 million (2016 £364.6 million). Refer to Note 8(b) for further details on the impairment testing performed on goodwill.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

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

#### (e) RETIREMENT BENEFITS

The group operates two defined benefit schemes for its employees which are accounted for in accordance with IAS 19 'Employee Benefits' ("IAS 19") 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 actuaries and other specialists within the Iberdrola group.

At 31 December 2017, the liability in the balance sheet for retirement benefit obligations amounted to £564.8 million (2016 £442.5 million). Sensitivity disclosures relating to the group's retirement benefit obligations are set out in Note 18.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 6 BUSINESS SEGMENT REPORTING

#### (a) Operating segments, business functions and business divisions

The group classifies its operating segments based on a combination of factors, principally differences in products and services and the regulatory environment in which each business operates. The group is organised into three reportable segments; Energy Networks, Energy Wholesale and Retail, and Renewables. The group identifies SPT, SPD and SPM as individual operating segments, but as management deem these operating segments to exhibit similar economic characteristics, they have been aggregated (together with other Energy Networks entities) into a single reported segment, Energy Networks. In line with IFRS 8 the group reports its segments on this basis and the measure of profit used for the purpose of reporting to the Chief Operating Decision maker ("CODM") is operating profit as per the consolidated income statement. All revenue for the reported segments arise from operations within Great Britain and Ireland. Revenue arising from operations within the Republic of Ireland is not deemed material enough to disclose as a separate operating segment.

In accordance with the disclosure requirements of IFRS 8, the Annual Report and Accounts of the group reports the relevant financial results of the reported segments as described above. In the interest of improved transparency, the group has voluntarily disclosed revenue and operating profit for the separate business divisions within the Energy Wholesale and Retail and Renewables reported segments, whilst also providing detail in relation to non-recurring items and certain remeasurements 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 reported segments, business functions and business divisions are as follows:

Reported segment	Business function	Business division	Business division description
Energy Networks		Energy Networks	The transmission and distribution business within the group.
Energy Wholesale and Retail	Energy Wholesale	Generation – Licensed business <sup>1</sup>	The licensed activity of the Energy Wholesale business function, which owns and operates gas and hydro-electric generation plant, and, until 24 March 2016, coal generation.
		Energy Management <sup>1</sup>	The non-licensed activities of the Energy Wholesale business function, responsible for wholesale market sales and purchases for the Generation and Supply licensed business divisions.
		Other	The other non-licensed activity of the Energy Wholesale business function which includes the results of the group's waste water treatment facility.
	Energy Retail	Supply – Licensed business <sup>1</sup>	The licensed activity of the Energy Retail business function responsible for the supply of electricity and gas to domestic and non-domestic customers.
		Other	The non-licensed activity of the Energy Retail business function includes the group's Energy Services activities and non-licensed metering activities, including smart meter asset provision.
Renewables		Renewables – Licensed business <sup>1</sup>	The Great Britain licensed activity of the Renewables reported segment, which develops and operates renewable generation plant, other than hydro-electric generation plant.
		Other	The non-licensed activity of the Renewables reported segment, which includes generation activity outside Great Britain until 1 August 2017 and the impact of the amortisation of the fair value attributed to the Renewables operating segment when purchased by Iberdrola during 2007.

<sup>1</sup> The Generation – Licensed, Supply – Licensed, Renewables – 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.aspx](http://www.scottishpower.com/pages/company_reporting.aspx).

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 6 BUSINESS SEGMENT REPORTING *continued*

### (b) Revenue by reported segment, business function and business division

#### (i) Revenue by reported segment

The revenue by reported segment for the year ended 31 December 2017 is detailed below.

Reported segment	External revenue £m	Inter-segment revenue £m	Revenue reported to the CODM <sup>*</sup> £m
Energy Networks	920.6	150.4 <sup>*</sup>	1,071.0
Energy Wholesale and Retail	4,265.9	6.9	4,272.8
Renewables	52.6	420.6	473.2
Elimination of inter-segment revenue			(577.9)
			5,239.1

<sup>\*</sup> Inter-segment revenue relating to Energy Networks is predominantly subject to regulation and is based on published tariffs set by Ofgem.

The revenue by reported segment for the year ended 31 December 2016 is detailed below.

Reported segment	External revenue <sup>**</sup> £m	Inter-segment revenue £m	Revenue reported to the CODM <sup>**</sup> £m
Energy Networks	905.4	174.4 <sup>*</sup>	1,079.8
Energy Wholesale and Retail	4,191.1	5.2	4,196.3
Renewables	46.1	300.7	346.8
Elimination of inter-segment revenue			(480.3)
			5,142.6

<sup>\*</sup> Inter-segment revenue relating to Energy Networks is predominantly subject to regulation and is based on published tariffs set by Ofgem.

<sup>\*\*</sup> Comparative figures have been restated (refer to Note 2).

#### (ii) Additional information – Revenue by business function and business division

The revenue by business function and business division for the year ended 31 December 2017 is detailed below:

Reported segment	Business function	Business division	Revenue £m	Joint venture share of revenue (Note (iii)) £m	Revenue re-allocations as per regulatory licence requirements (Note (iv)) £m	Revenue as per regulatory licence requirements £m
Energy Networks			1,071.0	–	–	1,071.0
		Generation – Licensed business	629.0	–	–	629.0
		Energy Management	3,371.3	–	–	3,371.3
		Elimination of intra-function revenue	(783.0)	–	–	(783.0)
		Netting adjustment <sup>*</sup>	(749.4)	–	–	(749.4)
	Energy Wholesale		2,467.9	–	–	2,467.9
		Supply – Licensed business	3,754.2	–	(35.5)	3,718.7
		Other	27.9	–	–	27.9
		Elimination of intra-function revenue	(11.7)	–	–	(11.7)
	Energy Retail		3,770.4	–	(35.5)	3,734.9
		Elimination of intra-segment revenue	(1,965.5)	–	–	(1,965.5)
Energy Wholesale and Retail			4,272.8	–	(35.5)	4,237.3
		Renewables – Licensed business	459.1	8.1	–	467.2
		Other	14.1	0.7	–	14.8
Renewables			473.2	8.8	–	482.0
Elimination of inter-segment revenue			(577.9)	–	–	(577.9)
Total			5,239.1	8.8	(35.5)	5,212.4

<sup>\*</sup> Refer to Note 2 (A1.2).

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 6 BUSINESS SEGMENT REPORTING *continued*

### (b) Revenue by reported segment, business function and business division *continued*

#### (ii) Additional information – Revenue by business function and business division *continued*

The revenue by business function and business division for the year ended 31 December 2016 is detailed below.

Reported segment	Business function	Business division	Revenue* £m	Joint venture share of revenue (Note (iii)) £m	Revenue re-allocations as per regulatory licence requirements (Note (iv)) £m	Revenue as per regulatory licence requirements* £m
Energy Networks			1,079.8	–	–	1,079.8
		Generation – Licensed business	719.1	–	–	719.1
		Energy Management	3,443.4	–	–	3,443.4
		Elimination of intra-function revenue	(990.8)	–	–	(990.8)
		Netting adjustment**	(854.5)	–	–	(854.5)
	Energy Wholesale		2,317.2	–	–	2,317.2
		Supply – Licensed business	3,702.4	–	(24.8)	3,677.6
		Other	9.6	–	–	9.6
	Energy Retail		3,712.0	–	(24.8)	3,687.2
		Elimination of intra-segment revenue	(1,832.9)	–	–	(1,832.9)
Energy Wholesale and Retail			4,196.3	–	(24.8)	4,171.5
		Renewables – Licensed business	331.8	7.9	–	339.7
		Other	15.0	–	–	15.0
Renewables			346.8	7.9	–	354.7
Elimination of inter-segment revenue			(480.3)	–	–	(480.3)
Total			5,142.6	7.9	(24.8)	5,125.7

\* Comparative figures have been restated (refer to Note 2).

\*\* Refer to Note 2 (A1.2).

(iii) All joint ventures within the group are consolidated using the equity method. The results of the joint ventures are therefore presented within Results of companies accounted for using the equity method on the face of the consolidated income statement and so do not form part of Revenue. As per the licence conditions, and the associated regulatory reporting, the group is required to proportionally consolidate the results of the joint ventures and so present revenues and costs in the appropriate lines of the income statement.

(iv) As disclosed in Note 26 of the financial statements, in line with group accounting policy, Taxes other than income tax includes the costs of the WHD scheme. As per the licence conditions, these costs are required to be deducted from Revenue.

### (c) Operating profit/(loss) by reported segment, business function and business division

#### (i) Operating profit/(loss) by reported segment

The operating profit/(loss) by reported segment for the year ended 31 December 2017 is detailed below.

Reported segment	Operating profit/(loss) reported to the CODM £m
Energy Networks	538.9
Energy Wholesale and Retail	(61.3)
Renewables	190.5
Unallocated	(14.3)
Total	653.8

The operating profit/(loss) by reported segment for the year ended 31 December 2016 is detailed below.

Reported segment	Operating profit/(loss) reported to the CODM £m
Energy Networks	577.2
Energy Wholesale and Retail	151.7
Renewables	103.8
Unallocated	(1.4)
Total	831.3

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 6 BUSINESS SEGMENT REPORTING *continued*

### (c) Operating profit/(loss) by reported segment, business function and business division *continued*

#### (ii) Additional information – Operating profit/(loss) by business function and business division

The operating profit/(loss) by business function and business division for the year ended 31 December 2017 is detailed below.

Reported segment	Business function	Business division	Operating profit/(loss) £m	Joint venture share of operating profit/(loss) (Note (iii)) £m	Non-recurring items (Note (iv)) £m	Certain remeasurements (Note (vi)) £m	Adjusted operating profit/(loss) as per regulatory licence requirements* £m
<b>Energy Networks</b>			<b>538.9</b>	<b>(0.1)</b>	<b>10.6</b>	<b>–</b>	<b>549.4</b>
		Generation – Licensed business	(12.8)	–	1.2	0.1	(11.5)
		Energy Management	(30.3)	–	0.7	24.4	(5.2)
		Other	3.6	–	0.1	–	3.7
	<b>Energy Wholesale</b>		<b>(39.5)</b>	<b>–</b>	<b>2.0</b>	<b>24.5</b>	<b>(13.0)</b>
		Supply – Licensed business	(21.8)	–	12.1	0.1	(9.6)
		Other	–	–	5.4	–	5.4
	<b>Energy Retail</b>		<b>(21.8)</b>	<b>–</b>	<b>17.5</b>	<b>0.1</b>	<b>(4.2)</b>
<b>Energy Wholesale and Retail</b>			<b>(61.3)</b>	<b>–</b>	<b>19.5</b>	<b>24.6</b>	<b>(17.2)</b>
		Renewables – Licensed business	213.8	1.3	0.7	–	215.8
		Other	(23.3)	0.2	0.1	–	(23.0)
<b>Renewables</b>			<b>190.5</b>	<b>1.5</b>	<b>0.8</b>	<b>–</b>	<b>192.8</b>
<b>Unallocated</b>			<b>(14.3)</b>	<b>–</b>	<b>13.7</b>	<b>–</b>	<b>(0.6)</b>
<b>Total</b>			<b>653.8</b>	<b>1.4</b>	<b>44.6</b>	<b>24.6</b>	<b>724.4</b>

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

The operating profit/(loss) by business function and business division for the year ended 31 December 2016 is detailed below.

Reported segment	Business function	Business division	Operating profit/(loss) £m	Joint venture share of operating profit/(loss) (Note (iii)) £m	Non-recurring items (Note (iv)) £m	Certain remeasurements (Note (vi)) £m	Adjusted operating profit/(loss) as per regulatory licence requirements* £m
<b>Energy Networks</b>			<b>577.2</b>	<b>0.1</b>	<b>5.2</b>	<b>–</b>	<b>582.5</b>
		Generation – Licensed business	(33.2)	–	3.5	(17.2)	(46.9)
		Energy Management	71.9	–	–	(58.9)	13.0
		Other	3.3	(0.1)	–	–	3.2
	<b>Energy Wholesale</b>		<b>42.0</b>	<b>(0.1)</b>	<b>3.5</b>	<b>(76.1)</b>	<b>(30.7)</b>
		Supply – Licensed business	114.3	–	16.8	(1.3)	129.8
		Other	(4.6)	–	3.7	–	(0.9)
	<b>Energy Retail</b>		<b>109.7</b>	<b>–</b>	<b>20.5</b>	<b>(1.3)</b>	<b>128.9</b>
<b>Energy Wholesale and Retail</b>			<b>151.7</b>	<b>(0.1)</b>	<b>24.0</b>	<b>(77.4)</b>	<b>98.2</b>
		Renewables – Licensed business	116.4	0.4	6.0	–	122.8
		Other	(12.6)	1.7	–	–	(10.9)
<b>Renewables</b>			<b>103.8</b>	<b>2.1</b>	<b>6.0</b>	<b>–</b>	<b>111.9</b>
<b>Unallocated</b>			<b>(1.4)</b>	<b>–</b>	<b>(0.7)</b>	<b>–</b>	<b>(2.1)</b>
<b>Total</b>			<b>831.3</b>	<b>2.1</b>	<b>34.5</b>	<b>(77.4)</b>	<b>790.5</b>

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

#### (iii) Joint venture share of operating profit

All joint ventures within the group are consolidated using the equity method. The results of the joint ventures are therefore presented within Results of companies accounted for using the equity method on the face of the consolidated income statement and so do not form part of Operating profit.

As per the licence conditions, and the associated regulatory reporting, the group is required to proportionally consolidate the results of the joint ventures and so presents revenues and costs in the appropriate lines of the income statement.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 6 BUSINESS SEGMENT REPORTING *continued*

### (c) Operating profit/(loss) by reported segment, business function and business division *continued*

#### (iv) Non-recurring items

In the year ended 31 December 2017 the following non-recurring items were recorded:

**Provisions for restructuring and other liabilities:** On review of the group's provisions as at 31 December 2017, net restructuring provisions and associated pension costs of £35.0 million were recognised principally in relation to a group-wide restructuring programme.

**Impairment and non-current asset write-offs:** During the year ended 31 December 2017 the group recognised an impairment charge of £1.2 million which primarily comprised the write-off of operational wind farm assets following fire damage. Non-current asset write-offs of £4.5 million were also recognised.

**Non-recurring costs/income:** During the year ended 31 December 2017 the group recognised £5.9 million of non-recurring costs and £2.0 million of non-recurring income on the settlement of various contractual disputes.

In the year ended 31 December 2016 the following non-recurring items were recorded:

**Provisions for restructuring and other liabilities:** On review of the group's provisions as at 31 December 2016, net restructuring provisions and associated pension costs of £21.9 million were recognised principally in relation to a restructuring programme within the Energy Retail business function.

**Impairment and non-current asset write-offs:** During the year ended 31 December 2016 the group recognised an impairment charge of £14.6 million comprising of a charge of £6.9 million following a reduction to the residual value of Longannet, a charge of £3.1 million for the write-off of operational wind farm assets following fire damage and a charge of £4.6 million in relation to the cancellation of certain onshore wind power projects (refer to Note 9). Non-current asset write-offs of £1.9 million were also recognised.

**Non-recurring income:** During the year the group recognised £3.9 million of non-recurring income on settlement of various contractual disputes.

#### (v) Certain remeasurements

Certain remeasurements are the fair value movements on energy contracts arising from the application of IAS 39. These have been disclosed separately to aid the understanding of the underlying performance of the group.

### (d) Other financial data by operating segment

Other items by reported segment for the year ended 31 December 2017	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
Energy Networks	732.6	249.8	0.6
Energy Wholesale and Retail	208.2	104.5	58.6
Renewables	737.7	125.5	–
Unallocated	21.9	18.5	0.1
<b>Total</b>	<b>1,700.4</b>	<b>498.3</b>	<b>59.3</b>

Other items by reported segment for the year ended 31 December 2016	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
Energy Networks	767.1	236.9	0.3
Energy Wholesale and Retail	115.7	118.2	81.1
Renewables	811.0	114.7	–
Unallocated	36.2	19.2	0.1
<b>Total</b>	<b>1,730.0</b>	<b>489.0</b>	<b>81.5</b>

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 7 GROUP INFORMATION

### (a) Subsidiaries and joint ventures

The table below sets out details of the subsidiaries and joint ventures of the group and the company as at 31 December. These are all included in the consolidated Accounts for the group. All entities are indirect holdings unless specified. Shares owned by the group are all ordinary shares.

Name	Principal activities	Registered office and country of incorporation (Note (xv))	Equity interest	
			2017	2016
<b>Energy Networks</b>				
<b>Subsidiaries</b>				
Scottish Power Energy Networks Holdings Limited	Holding company	(A)	100% (i)	100%
SP Distribution plc	Ownership and operation of distribution network within the ScottishPower area	(A)	100%	100%
SP Manweb plc	Ownership and operation of distribution network within the Mersey and North Wales area	(B)	100%	100%
SP Network Connections Limited	Design and construction of utility connections	(B)	100%	100%
SP Power Systems Limited	Provision of asset management services and multi-utility and construction service	(A)	100%	100%
SP Transmission plc	Ownership and operation of transmission network within the ScottishPower area	(A)	100%	100%
Manweb Services Limited	Operation of a private electricity distribution network	(B)	100%	100%
<b>Joint ventures</b>				
NGET/SPT Upgrades Limited	Development of offshore HVDC West Coast transmission link	(C)	50% (ii), (iii)	50%
<b>Energy Wholesale and Retail</b>				
<b>Subsidiaries</b>				
Scottish Power Generation Holdings Limited	Holding company	(D)	100% (i)	100%
ScottishPower (DCL) Limited	Holding company	(B)	100%	100%
ScottishPower Energy Management Limited	Wholesale energy management company engaged in purchase and sale of electricity and gas	(D)	100%	100%
ScottishPower Energy Management (Agency) Limited	Agent for energy management activity of ScottishPower Energy Management Limited and Scottish Power UK plc	(D)	100%	100%
ScottishPower Generation Limited	Electricity generation	(D)	100%	100%
ScottishPower (SCPL) Limited	Holding company	(B)	100%	100%
SMW Limited	Waste water treatment	(D)	100%	100%
SP Gas Transportation Cockenzie Limited	Holder of Gas Transporter Licence	(D)	100%	100%
SP Gas Transportation Hatfield Limited	Holder of Gas Transporter Licence	(D)	100%	100%
ScottishPower Energy Retail Limited	Supply of electricity and gas to domestic and business customers	(D)	100%	100%
SP Dataserve Limited	Data collection, data aggregation, meter operation and revenue protection	(D)	100%	100%
SP Smart Meter Assets Limited	Provider of smart meter assets	(D)	100% (iv)	–
<b>Joint ventures</b>				
ScotAsh Limited	Sales of ash and ash-related cementitious products	(E)	– (ii), (v)	50%
<b>Renewables</b>				
<b>Subsidiaries</b>				
ScottishPower Renewable Energy Limited	Holding company	(D)	100% (i)	100%
Coldham Windfarm Limited	Electricity generation	(B)	80%	80%
East Anglia One Limited	Development and construction of offshore wind farm	(F)	100%	100%
East Anglia One North Limited	Development of offshore wind farm	(F)	100% (vi)	–
East Anglia Two Limited	Development of offshore wind farm	(F)	100% (vi)	–
East Anglia Three Limited	Development of offshore wind farm	(F)	100% (vii)	100%
ScottishPower Renewables (UK) Limited	Development, construction and operation of wind farms	(G)	100%	100%
ScottishPower Renewables (WODS) Limited	Operation of offshore wind farm	(D)	100%	100%
Iberdrola Renovables France SAS	Holding company	(H)	– (viii)	100%
Iberdrola Renovables Offshore Deutschland GmbH	Development and construction of offshore wind farm	(I)	– (ix), (x)	100%
Iberdrola Renovables Deutschland GmbH	Holding company	(I)	– (ix)	100%
Ailes Marines SAS	Development of offshore wind farm	(H)	– (viii)	70%
<b>Joint ventures</b>				
CeltPower Limited	Electricity generation	(B)	50% (ii)	50%
East Anglia Offshore Wind Limited	Commercial operation of offshore met masts	(F)	50% (ii)	50%
Norfolk Vanguard Limited (formally known as East Anglia Four Limited)	Development of offshore wind farm	(J)	– (ii), (xi)	–
Morecambe Wind Limited	Provision of operational services	(K)	50% (ii)	50%



# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 7 GROUP INFORMATION *continued*

### (a) Subsidiaries and joint ventures *continued*

(a) Subsidiaries and joint ventures continued

Name	Principal activities	Registered office and country of incorporation (Note (xv))	Equity interest	
			2017	2016
Other				
Subsidiaries				
ScottishPower Investments Limited	Holding company	(D)	100%	(i) 100%
Dormant subsidiaries in liquidation				
Demon Internet Limited	In liquidation	(L)	100%	100%
Manweb Energy Consultants Limited	In liquidation	(L)	100%	100%
Manweb Nominees Limited	In liquidation	(L)	100%	100%
Manweb Share Scheme Trustees Limited	In liquidation	(L)	100%	100%
SP Gas Limited	In liquidation	(M)	100%	(xii) 100%
Dormant subsidiaries now dissolved				
Clubcall Telephone Services Limited	Dissolved	(N)	–	(xiii) 100%
Clubline Services Limited	Dissolved	(B)	–	(xiii) 100%
Manweb Pensions Trustees Limited	Dissolved	(L)	–	(xiii) 100%
ScottishPower (DCOL) Limited	Dissolved	(O)	–	(xiii) 100%
Teledata (Holdings) Limited	Dissolved	(P)	–	(xiii) 100%
Teledata (Outsourcing) Limited	Dissolved	(N)	–	(xiii) 100%
Teledata Scotland Limited	Dissolved	(P)	–	(xiii) 100%
The Callcentre Service Limited	Dissolved	(N)	–	(xiii) 100%
The Information Service Limited	Dissolved	(N)	–	(xiii) 100%

(i) The investment in this company is a direct holding of Scottish Power UK plc at 31 December 2017.

(ii) All joint ventures are accounted for using the equity method.

(iii) NGET/SPT Upgrades Limited has a non-coterminous year end date of 31 March. This is a contractual obligation as agreed in the joint operating agreement.

(iv) SP Smart Meter Assets Limited was incorporated on 9 January 2017 and is a direct subsidiary of Scottish Power Generation Holdings Limited.

(v) On 19 July 2017, the group sold its 50% interest in share capital of ScotAsh Limited (refer to Note 10).

(vi) East Anglia One North Limited and East Anglia Two Limited were incorporated on 21 December 2017 and are direct subsidiaries of ScottishPower Renewables (UK) Limited.

(vii) On 15 February 2016, the group acquired the remaining 50% interest in the share capital of East Anglia Three Limited, at which point East Anglia Three Limited ceased to be a joint venture and became a subsidiary.

(viii) On 1 August 2017, the group sold its entire interest in the share capital of Iberdrola Renovables France SAS (refer to Note 36). Iberdrola Renovables France SAS has a 70% equity holding in one subsidiary, Ailes Marines SAS.

(ix) On 1 August 2017, the group sold its entire interest in the share capital of Iberdrola Renovables Deutschland GmbH (refer to Note 36). Iberdrola Renovables Deutschland GmbH wholly owns two subsidiaries: Iberdrola Renovables Offshore Deutschland GmbH and Baltic Eagle GmbH (see footnote (xiv) below).

(x) On 3 December 2015, Iberdrola Renovables Offshore Deutschland GmbH entered into a joint operation with 50Hertz Offshore GmbH. The agreement is for the joint realisation of the offshore substation being built as part of the Wiking offshore wind farm project located in Germany. Both parties have joint control of this asset. As noted at (ix) above, the group no longer has an interest in this joint operation.

(xi) On 15 February 2016, the group sold its 50% interest in the share capital of East Anglia Four Limited for a consideration of £0.50, being the carrying value of the investment. The group now holds no interest in East Anglia Four Limited.

(xii) The investment in SP Gas Limited is held 50% directly by the company and 50% by another company within the group.

(xiii) This company was dissolved during the year ended 31 December 2017.

(xiv) On 21 February 2017, Iberdrola Renovables Deutschland GmbH acquired the entire share capital of Baltic Eagle GmbH. The group no longer has an interest in this entity (see footnote (ix) above).

(xv) The registered offices of the subsidiaries and joint ventures are as listed below, along with their countries of incorporation. Where a company's registered office is in England it is registered in England and Wales:

- (A) Ochil House, 10 Technology Avenue, Hamilton International Technology Park, Blantyre G72 0HT, Scotland
- (B) 3 Prenton Way, Prenton, CH43 3ET, England
- (C) 1–3 Strand, London, WC2N 5EH, England
- (D) 320 St. Vincent Street, Glasgow G2 5AD, Scotland
- (E) Portland House, Bickenhall Lane, Solihull, Birmingham, B37 7BQ, England
- (F) 3rd Floor, 1 Tudor Street, London, EC4Y 0AH, England
- (G) The Soloist, 1 Lanyon Place, Belfast, BT1 3LP, Northern Ireland
- (H) 40 Rue de la Boetie, 75008, Paris, France

- (I) Charlottenstrasse 63, D-10117, Berlin, Germany
- (J) 1st Floor, 1 Tudor Street, London, EC4Y 0AH, England
- (K) 5 Howick Place, London, SW1P 1WG, England
- (L) Johnston Carmichael, 107–111 Fleet Street, London, EC4A 2AB, England
- (M) Johnston Carmichael, 227 West George Street, Glasgow G2 2ND, Scotland
- (N) KPMG LLP, 15 Canada Square, London, E14 5GL, England
- (O) KPMG LLP, 8 Salisbury Square, London, EC4Y 8BB, England
- (P) KPMG LLP, Saltire Court, 20 Castle Terrace, Edinburgh, EH1 2EG, Scotland

For those entities incorporated in Scotland, Northern Ireland and England and Wales, the principal place of business is considered to be the United Kingdom; for all other entities, the country of incorporation is the principal place of business.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 7 GROUP INFORMATION *continued*

### (b) Judgements and assumptions used to determine the scope of the consolidation

The consolidated financial statements combine the financial statements of Scottish Power UK plc and its subsidiaries. A subsidiary is an entity over which the company has control. The company has control over another entity when it has power over the relevant activities of the investee, for example through voting rights; exposure, or rights to, variable returns from its involvement with the investee; and the ability to affect those returns through its power over the investee.

No significant judgements have been made in applying these principles during the year.

### (c) Significant restrictions

As is typical for a group of its size and scope, there are restrictions on the ability of the group to obtain distributions of capital, access the assets or repay the liabilities of members of its group due to the statutory, regulatory and contractual requirements of its subsidiaries and due to the protective rights of non-controlling interests. After consideration of these factors, the resulting significant restrictions have been identified:

#### SP Distribution plc

SP Distribution plc is a regulated DNO whose activities are governed by a licence granted by Ofgem. For such licenced entities the main drivers facilitating distributions including dividends is holding an investment grade credit rating and complying with several other licence conditions. The total value of distributable reserves is restricted by the requirement to comply with several licence conditions including holding an investment grade credit rating. In addition, standard condition 26 of the distribution licence conditions restricts the disposal of property, plant and equipment.

Value restricted	2017 £m	2016 £m
Distributable reserves	571.0	557.6
Property, plant and equipment	2,729.9	2,633.1

#### SP Manweb plc

SP Manweb plc is a regulated DNO whose activities are governed by a licence granted by Ofgem. For such licenced entities the main drivers facilitating distributions including dividends is holding an investment grade credit rating and complying with several other licence conditions. The total value of distributable reserves is restricted by the requirement to comply with several licence conditions including holding an investment grade credit rating. In addition, standard condition 26 of the distribution licence conditions restricts the disposal of property, plant and equipment.

Value restricted	2017 £m	2016 £m
Distributable reserves	690.0	681.6
Property, plant and equipment	2,721.4	2,577.1

#### SP Transmission plc

SP Transmission plc is a regulated electricity transmission entity whose activities are governed by a licence granted by Ofgem. For such licenced entities the main drivers facilitating distributions including dividends is holding an investment grade credit rating and complying with several other licence conditions. The total value of distributable reserves is restricted by the requirement to comply with several licence conditions including holding an investment grade credit rating. In addition, standard condition B3 of the transmission licence conditions restricts the disposal of property, plant and equipment.

Value restricted	2017 £m	2016 £m
Distributable reserves	644.2	572.6
Property, plant and equipment	2,696.2	2,466.2

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 8 INTANGIBLE ASSETS

### (a) Movements in intangible assets

Year ended 31 December 2016	Note	Goodwill (Note (b)) £m	Other intangible assets			Total £m	Total £m
			Computer software (Note (i)) £m	Licences £m	Other (Note (ii)) £m		
<b>Cost:</b>							
At 1 January 2016		364.6	395.9	9.5	284.4	689.8	1,054.4
Additions		–	43.3	–	–	43.3	43.3
Transfers from/(to) property, plant and equipment	(ii)	–	2.0	–	(282.9)	(280.9)	(280.9)
Disposals		–	(42.0)	–	–	(42.0)	(42.0)
<b>At 31 December 2016</b>		<b>364.6</b>	<b>399.2</b>	<b>9.5</b>	<b>1.5</b>	<b>410.2</b>	<b>774.8</b>
<b>Amortisation:</b>							
At 1 January 2016		–	200.5	2.9	0.2	203.6	203.6
Amortisation for the year		–	59.8	0.4	0.4	60.6	60.6
Transfers from property, plant and equipment		–	1.4	–	–	1.4	1.4
Disposals		–	(41.8)	–	–	(41.8)	(41.8)
<b>At 31 December 2016</b>		<b>–</b>	<b>219.9</b>	<b>3.3</b>	<b>0.6</b>	<b>223.8</b>	<b>223.8</b>
<b>Net book value:</b>							
At 31 December 2016		364.6	179.3	6.2	0.9	186.4	551.0
At 1 January 2016		364.6	195.4	6.6	284.2	486.2	850.8

Year ended 31 December 2017	Note	Goodwill (Note (b)) £m	Other intangible assets			Total £m	Total £m
			Computer software (Note (i)) £m	Licences £m	Other (Note (ii)) £m		
<b>Cost:</b>							
At 1 January 2017		364.6	399.2	9.5	1.5	410.2	774.8
Group restructuring	(iii)	–	–	–	(0.4)	(0.4)	(0.4)
Additions		–	44.5	–	–	44.5	44.5
Transfers from property, plant and equipment		–	0.5	–	–	0.5	0.5
Disposals		–	(6.3)	–	–	(6.3)	(6.3)
<b>At 31 December 2017</b>		<b>364.6</b>	<b>437.9</b>	<b>9.5</b>	<b>1.1</b>	<b>448.5</b>	<b>813.1</b>
<b>Amortisation:</b>							
At 1 January 2017		–	219.9	3.3	0.6	223.8	223.8
Amortisation for the year		–	59.5	0.3	0.4	60.2	60.2
Transfers from property, plant and equipment		–	0.2	–	–	0.2	0.2
Disposals		–	(6.2)	–	–	(6.2)	(6.2)
<b>At 31 December 2017</b>		<b>–</b>	<b>273.4</b>	<b>3.6</b>	<b>1.0</b>	<b>278.0</b>	<b>278.0</b>
<b>Net book value:</b>							
At 31 December 2017		364.6	164.5	5.9	0.1	170.5	535.1
At 1 January 2017		364.6	179.3	6.2	0.9	186.4	551.0

- (i) The cost of fully amortised computer software still in use at 31 December 2017 was £30.6 million (2016 £30.8 million).
- (ii) The 'Other' category of intangible assets at 1 January 2016 principally represented the value attributable to future Renewables projects recognised by Iberdrola, S.A. on acquisition of SPREL. During 2016, following FID approval of the East Anglia One project, these assets were transferred to 'Property, plant and equipment' (refer to Note 9).
- (iii) Group restructuring of £0.4 million in 2017 relates to the disposal of the group's operations in France and Germany (refer to Note 36).
- (iv) The cost of intangible assets under construction at 31 December 2017 was £72.4 million (2016 £49.5 million).

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 8 INTANGIBLE ASSETS *continued*

#### (b) Impairment test for goodwill

The carrying amount of goodwill for the Renewables business at 31 December 2017 was £364.6 million (2016 £364.6 million).

The recoverable amount for the Renewables business has been determined based on a value-in-use calculation. The calculation uses cash flow projections which reflect past experience and which are based upon a management approved business plan ending in 2024. Cash flows beyond that period reflect asset estimated useful lives as well as management's forward view of 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.

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. The output is valued at forward power prices based on: observable market information where available; assumed continuing government support through ROCs, CfDs and other mechanisms; and on internal model assumptions. Cash outflows are based on planned operating and capital maintenance expenditure.

The main assumptions and basis for determining values assigned to the key assumptions are detailed below.

Main assumptions used for value-in-use calculations	Basis for determining values assigned to key assumptions
Discount rate (pre-tax): Onshore 5.95%; and Offshore 6.85%	Discount rate is determined on the basis of market data and the divisional cost of capital
Forward price of power	Market quotes/management future expectations

The value-in-use calculation of the Renewables business exceeds the carrying value.

The group has also performed several sensitivity analyses of the impairment test result in relation to the key assumptions to which the value-in-use calculation is most sensitive, these tests included:

- 1% increase in the discount rate;
- 10% decrease in the power price per kWh (Kilowatt hour) (only applicable to production for which no long-term sales agreements have been entered into); and
- a 5% decrease in energy output.

The sensitivity analysis results showed:

- a 1% increase in the discount rate would result in an impairment charge of £35 million;
- a 10% decrease in the power price would result in the value-in-use still exceeding the carrying value; and
- a 5% decrease in energy output would result in an impairment charge of £80 million.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 9 PROPERTY, PLANT AND EQUIPMENT

### (a) Movements in property, plant and equipment

	Notes	Total operating plant (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
<b>Year ended 31 December 2016</b>						
<b>Cost:</b>						
At 1 January 2016		13,869.1	354.9	1,725.1	20.5	15,969.6
Additions		98.3	17.5	1,562.2	8.7	1,686.7
Transfers		(1.6)	1.6	–	–	–
Transfers from in progress to plant in use		878.6	24.3	(891.4)	(11.5)	–
Transfers from a joint venture	(i)	–	–	19.0	–	19.0
Transfer to inventory in respect of offshore transmission asset		–	–	(9.5)	–	(9.5)
Net transfers (to)/from intangible assets	(ii)	(2.0)	–	282.9	–	280.9
Disposals		(1,067.6)	(32.7)	–	(0.8)	(1,101.1)
Impairment	(iii)	(4.0)	–	(4.2)	(0.4)	(8.6)
Exchange		–	–	58.7	–	58.7
<b>At 31 December 2016</b>		<b>13,770.8</b>	<b>365.6</b>	<b>2,742.8</b>	<b>16.5</b>	<b>16,895.7</b>
<b>Depreciation:</b>						
At 1 January 2016		4,578.2	144.6	–	–	4,722.8
Charge for the year		399.4	14.4	–	–	413.8
Transfers to intangible assets		(1.4)	–	–	–	(1.4)
Disposals		(1,044.2)	(30.4)	–	–	(1,074.6)
Impairment	(iii)	6.0	–	–	–	6.0
<b>At 31 December 2016</b>		<b>3,938.0</b>	<b>128.6</b>	<b>–</b>	<b>–</b>	<b>4,066.6</b>
<b>Net book value:</b>						
<b>At 31 December 2016</b>		<b>9,832.8</b>	<b>237.0</b>	<b>2,742.8</b>	<b>16.5</b>	<b>12,829.1</b>
<b>At 1 January 2016</b>		<b>9,290.9</b>	<b>210.3</b>	<b>1,725.1</b>	<b>20.5</b>	<b>11,246.8</b>
The net book value of property, plant and equipment at 31 December 2016 is analysed as follows:						
Property, plant and equipment in use		9,832.8	237.0	–	–	10,069.8
Property, plant and equipment in the course of construction		–	–	2,742.8	16.5	2,759.3
		<b>9,832.8</b>	<b>237.0</b>	<b>2,742.8</b>	<b>16.5</b>	<b>12,829.1</b>

	Notes	Total operating plant (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
<b>Year ended 31 December 2017</b>						
<b>Cost:</b>						
At 1 January 2017		13,770.8	365.6	2,742.8	16.5	16,895.7
Additions		161.0	18.6	1,434.3	42.0	1,655.9
Transfers from in progress to plant in use		1,644.8	3.3	(1,626.2)	(21.9)	–
Transfers to intangible assets		(0.5)	–	–	–	(0.5)
Disposals		(92.6)	(68.5)	(1.0)	(1.5)	(163.6)
Group restructuring	(iv)	–	(0.1)	(1,143.4)	–	(1,143.5)
Impairment	(iii)	(1.4)	–	(0.1)	(0.1)	(1.6)
Exchange		–	–	46.6	–	46.6
<b>At 31 December 2017</b>		<b>15,482.1</b>	<b>318.9</b>	<b>1,453.0</b>	<b>35.0</b>	<b>17,289.0</b>
<b>Depreciation:</b>						
At 1 January 2017		3,938.0	128.6	–	–	4,066.6
Charge for the year		422.5	14.4	–	–	436.9
Transfers to intangible assets		(0.2)	–	–	–	(0.2)
Disposals		(88.3)	(59.7)	–	–	(148.0)
Impairment	(iii)	(0.4)	–	–	–	(0.4)
<b>At 31 December 2017</b>		<b>4,271.6</b>	<b>83.3</b>	<b>–</b>	<b>–</b>	<b>4,354.9</b>
<b>Net book value:</b>						
<b>At 31 December 2017</b>		<b>11,210.5</b>	<b>235.6</b>	<b>1,453.0</b>	<b>35.0</b>	<b>12,934.1</b>
<b>At 1 January 2017</b>		<b>9,832.8</b>	<b>237.0</b>	<b>2,742.8</b>	<b>16.5</b>	<b>12,829.1</b>
The net book value of property, plant and equipment at 31 December 2017 is analysed as follows:						
Property, plant and equipment in use		11,210.5	235.6	–	–	11,446.1
Property, plant and equipment in the course of construction		–	–	1,453.0	35.0	1,488.0
		<b>11,210.5</b>	<b>235.6</b>	<b>1,453.0</b>	<b>35.0</b>	<b>12,934.1</b>

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 9 PROPERTY, PLANT AND EQUIPMENT *continued*

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

Year ended 31 December 2016	Hydro-electric plants £m	Fossil fuel plants £m	CCGTs £m	Wind power plants £m	Gas storage facilities £m	Transmission facilities £m	Distribution facilities £m	Meters and measuring devices £m	Other facilities (Note (vi)) £m	Total operating plant £m
<b>Cost:</b>										
At 1 January 2016	150.3	972.0	927.4	3,144.9	35.5	1,859.6	6,204.1	405.7	169.6	13,869.1
Additions	–	–	1.0	16.7	0.1	–	5.3	75.2	–	98.3
Transfers	–	(1.6)	–	–	–	–	–	–	–	(1.6)
Transfers from in progress to plant in use	2.3	–	11.4	259.7	–	275.5	328.3	–	1.4	878.6
Transfers to intangible assets	–	(2.0)	–	–	–	–	–	–	–	(2.0)
Disposals	–	(968.4)	(2.7)	(0.1)	–	(8.0)	(16.1)	(72.1)	(0.2)	(1,067.6)
Impairment	–	–	–	(4.0)	–	–	–	–	–	(4.0)
<b>At 31 December 2016</b>	<b>152.6</b>	<b>–</b>	<b>937.1</b>	<b>3,417.2</b>	<b>35.6</b>	<b>2,127.1</b>	<b>6,521.6</b>	<b>408.8</b>	<b>170.8</b>	<b>13,770.8</b>
<b>Depreciation:</b>										
At 1 January 2016	82.5	941.4	449.7	716.4	13.2	415.6	1,558.9	304.1	96.4	4,578.2
Charge for the year	4.8	0.2	49.1	103.7	0.8	46.9	167.4	19.3	7.2	399.4
Transfers	–	–	–	(18.1)	–	–	18.1	–	–	–
Transfers to intangible assets	–	(1.4)	–	–	–	–	–	–	–	(1.4)
Disposals	–	(947.1)	(2.4)	(0.1)	–	(7.3)	(15.3)	(71.9)	(0.1)	(1,044.2)
Impairment	–	6.9	–	(0.9)	–	–	–	–	–	6.0
<b>At 31 December 2016</b>	<b>87.3</b>	<b>–</b>	<b>496.4</b>	<b>801.0</b>	<b>14.0</b>	<b>455.2</b>	<b>1,729.1</b>	<b>251.5</b>	<b>103.5</b>	<b>3,938.0</b>
<b>Net book value:</b>										
At 31 December 2016	65.3	–	440.7	2,616.2	21.6	1,671.9	4,792.5	157.3	67.3	9,832.8
At 1 January 2016	67.8	30.6	477.7	2,428.5	22.3	1,444.0	4,645.2	101.6	73.2	9,290.9
<b>Year ended 31 December 2017</b>										
<b>Cost:</b>										
At 1 January 2017	152.6	–	937.1	3,417.2	35.6	2,127.1	6,521.6	408.8	170.8	13,770.8
Additions	–	–	0.4	30.7	0.1	–	4.4	85.1	40.3	161.0
Transfers	–	–	–	(10.3)	–	–	10.3	(93.5)	93.5	–
Transfers from in progress to plant in use	5.0	–	20.3	346.5	0.3	768.5	481.4	21.5	1.3	1,644.8
Transfers to intangible assets	(0.4)	–	–	–	–	–	–	–	(0.1)	(0.5)
Disposals	–	–	(19.3)	(0.1)	(0.1)	(9.1)	(24.2)	(37.7)	(2.1)	(92.6)
Impairment	–	–	–	(1.4)	–	–	–	–	–	(1.4)
<b>At 31 December 2017</b>	<b>157.2</b>	<b>–</b>	<b>938.5</b>	<b>3,782.6</b>	<b>35.9</b>	<b>2,886.5</b>	<b>6,993.5</b>	<b>384.2</b>	<b>303.7</b>	<b>15,482.1</b>
<b>Depreciation:</b>										
At 1 January 2017	87.3	–	496.4	801.0	14.0	455.2	1,729.1	251.5	103.5	3,938.0
Charge for the year	4.7	–	33.5	119.4	0.9	56.6	176.4	22.2	8.8	422.5
Transfers	–	–	–	(6.6)	–	–	6.6	(12.2)	12.2	–
Transfers to intangible assets	(0.2)	–	–	–	–	–	–	–	–	(0.2)
Disposals	–	–	(18.7)	(0.1)	(0.1)	(8.8)	(21.0)	(37.7)	(1.9)	(88.3)
Impairment	–	–	–	(0.4)	–	–	–	–	–	(0.4)
<b>At 31 December 2017</b>	<b>91.8</b>	<b>–</b>	<b>511.2</b>	<b>913.3</b>	<b>14.8</b>	<b>503.0</b>	<b>1,891.1</b>	<b>223.8</b>	<b>122.6</b>	<b>4,271.6</b>
<b>Net book value:</b>										
At 31 December 2017	65.4	–	427.3	2,869.3	21.1	2,383.5	5,102.4	160.4	181.1	11,210.5
At 1 January 2017	65.3	–	440.7	2,616.2	21.6	1,671.9	4,792.5	157.3	67.3	9,832.8

- (i) During 2016, Renewables finalised an agreement with Vattenfall Wind Power Ltd ("Vattenfall") to split the remainder of the East Anglia Zone. As part of this suite of agreements, £19.0 million of development assets were transferred from East Anglia Offshore Wind Limited (a joint venture between ScottishPower Renewables (UK) Limited and Vattenfall) to subsidiary companies within the group.
- (ii) This primarily represented future Renewables projects in the development phase (to which value was attributed on Iberdrola's acquisition of ScottishPower Renewable Energy Limited) that have been transferred from Intangible assets to Property, plant and equipment when the construction of each wind farm commenced (refer to Note 8).
- (iii) The impairment charge of £1.2 million made during the year ended 31 December 2017 primarily comprised the write-off of operational wind farm assets following fire damage. The impairment charge of £14.6 million made during the year ended 31 December 2016 comprised a £6.9 million reduction to the residual value of Longannet, following a review of the scrap value of the plant. Prior to the 2016 year end, the remaining plant assets in relation to Longannet were disposed of. The remaining impairment charge comprised the write-off of operational wind farm assets following fire damage of £3.1 million and a charge of £4.6 million in respect of the cancellation of certain onshore wind projects.
- (iv) Group restructuring of £1,143.5 million in 2017 relates to the disposal of the group's operations in France and Germany (refer to Note 36).
- (v) The Other facilities category of operating plant largely comprises waste water treatment facilities and Energy Networks communications facilities.
- (vi) Following a review, the group increased the useful life of its CCGT stations in 2017 (refer to Note 2).
- (vii) Interest on the funding attributable to major capital projects was capitalised during the year at a rate of 2.1% (2016 1.7%).
- (viii) The cost of fully depreciated property, plant and equipment still in use at 31 December 2017 was £622.0 million (2016 £673.3 million).
- (ix) Included within Other operating income in the income statement for the year ended 31 December 2017 is £1.7 million (2016 £6.9 million) relating to compensation receivable from third parties for items of property, plant and equipment that were impaired, lost or given up.
- (x) Included within the cost of property, plant and equipment at 31 December 2017 are assets in use not subject to depreciation, being land and cushion gas, of £135.5 million (2016 £139.3 million).

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 9 PROPERTY, PLANT AND EQUIPMENT *continued*

### (c) Operating lease arrangements

	2017 £m	2016 £m
<b>(i) Operating lease payments</b>		
Minimum lease payments under operating leases recognised as an expense in the year	25.6	21.9
Contingent based operating lease rents recognised as an expense in the year	58.1	56.3
Sublease payments recognised as an expense in the year	0.1	0.1
	<b>83.8</b>	<b>78.3</b>

The group leases various property, plant and equipment 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. Due to the nature of these contracts it is not possible to estimate the future obligation in relation to these contracts with sufficient reliability.

	2017 £m	2016 £m
<b>(ii) Operating lease commitments</b>		
The future minimum discounted lease payments under non-cancellable operating leases are as follows:		
Within one year	24.6	25.6
Between one and five years	76.3	74.0
More than five years	209.3	218.4
	<b>310.2</b>	<b>318.0</b>

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

	2017 £m	2016 £m
<b>(iii) Operating lease receivables</b>		
The future minimum discounted lease payments receivable under non-cancellable operating leases are as follows:		
Within one year	2.6	2.0
Between one and five years	2.6	1.5
More than five years	0.8	0.9
	<b>6.0</b>	<b>4.4</b>

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 sublease rentals recognised as income in the year ended 31 December 2017 amounted to £1.3 million (2016 £1.1 million).

### (d) Capital commitments

	2017 £m	2016 £m
Contracted but not provided	1,660.7	2,429.4

### (e) Research and development expenditure

The amount of research and development expenditure recognised as an expense during the year was £6.1 million (2016 £8.0 million).

## 10 INVESTMENTS IN JOINT VENTURES

### (a) Movements in investments in joint ventures are analysed as follows:

	Notes	Shares £m	Loans £m	Total £m
At 1 January 2016		12.7	18.4	31.1
Repayment of capital	(vi)	(5.2)	–	(5.2)
Repayment of loans		–	(18.1)	(18.1)
Share of result for year		0.9	–	0.9
At 1 January 2017		8.4	0.3	8.7
Repayment of capital	(vi)	(2.0)	–	(2.0)
Repayment of loans		–	(0.3)	(0.3)
Disposals	(vii)	(1.7)	–	(1.7)
Share of result for year		0.9	–	0.9
At 31 December 2017		<b>5.6</b>	<b>–</b>	<b>5.6</b>

(i) Investments in joint ventures are accounted for using the equity method. Details of the joint ventures are set out in Note 7.

(ii) No quoted market prices exist for investments in joint ventures.

(iii) No significant restrictions exist (e.g. resulting from borrowing arrangements, regulatory requirements or contractual arrangements between investors with joint control of or significant influence over a joint venture) that impact upon the ability of joint ventures to transfer funds to the group in the form of cash dividends, or to repay loans or advances made by the group (2016 none).

(iv) On 15 February 2016, the group acquired the remaining 50% of the share capital of East Anglia Three Limited for £0.50 at which point East Anglia Three Limited ceased to be a joint venture and became a subsidiary.

(v) On 15 February 2016, the group disposed of its 50% interest in the share capital of East Anglia Four Limited for a consideration equal to its carrying value of £0.50.

(vi) On 27 July 2016, the group's 50% joint venture, East Anglia Offshore Wind Limited repaid share capital of £5.2 million to the group. A further £2.0 million of share capital was repaid on 10 November 2017.

(vii) On 19 July 2017, the group sold its 50% interest in the share capital of ScotAsh Limited for a consideration of £1.6 million.

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 10 INVESTMENTS IN JOINT VENTURES *continued*

#### (b) Interest in joint ventures

	2017 £m	2016 £m
Aggregate carrying amount of individually immaterial equity accounted interests	5.6	8.4
Aggregate profit from continuing operations attributable to the group	0.9	0.9
Aggregate total comprehensive income attributable to the group	0.9	0.9

The group has no interests in associates.

#### (c) Commitments

The group has commitments not recognised as at 31 December 2017 relating to its interests in joint ventures of £98.4 million (2016 £200.8 million).

### 11 FINANCIAL INSTRUMENTS

#### (a) Carrying value of financial instruments

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

		2017		2016 Restated*	
	Notes	Carrying amount £m	Fair value £m	Carrying amount £m	Fair value £m
<b>Financial assets</b>					
Finance lease receivables		0.5	0.5	0.9	0.9
Derivative financial instruments	(i)	171.6	171.6	301.5	301.5
Current receivables	(ii)	1,399.9	1,399.9	1,505.4	1,505.4
Non-current receivables	(ii)	39.1	39.1	37.9	37.9
Other investments		1.1	1.1	1.1	1.1
Cash	(iii)	45.6	45.6	35.5	35.5
<b>Financial liabilities</b>					
Derivative financial instruments	(i)	(69.4)	(69.4)	(164.6)	(164.6)
Loans and other borrowings	(iv)	(5,667.8)	(6,280.9)	(6,883.0)	(7,412.7)
Payables	(ii)	(1,314.1)	(1,314.1)	(1,496.2)	(1,496.2)

\* Comparative figures have been restated (refer to Note 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 footnote (iv) below, which is categorised as Level 2 in the fair value hierarchy.

- (i) Further detail on derivative financial instruments is disclosed in Note 21.
- (ii) Balances outwith the scope of IFRS 7 have been excluded, namely prepayments, payments received on account and other taxes receivable and payable.
- (iii) As a general rule, cash deposited with banks earns interest at rates similar to market rates on daily deposits. Cash as at 31 December 2017 includes deposits with banks of £45.6 million (2016 £33.7 million) which is either restricted for use on specific projects, to meet regulatory requirements, or for use by a joint operation, and so is not available to finance the group's day-to-day operations.
- (iv) 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.

#### (b) Measurement of financial instruments

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.

In both the current and prior year all derivatives held by the group are Level 2.

Included in Level 2 liabilities of £69.4 million (2016 £164.6 million) are inseparable third-party credit enhancements. These have been reflected in the fair value measurement of the liability.

Level 2 commodity derivatives are fair valued by comparing and discounting the difference between the expected contractual cash flows for the relevant commodities and the quoted prices for those commodities in an active market.

Level 2 foreign exchange derivatives comprise cross currency swaps and forward foreign exchange contracts. Cross currency swaps and forward foreign exchange contracts are fair valued using forward exchange rates that are quoted in an active market.



# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 11 FINANCIAL INSTRUMENTS *continued*

### (c) Offsetting of financial assets and financial liabilities

The group is eligible to present financial assets and financial liabilities net on the balance sheet as described in Note 3G.5. The following table provides information on the impact of offsetting on the consolidated balance sheet as well as the financial impact of the netting of certain instruments in the event of default or similar agreements.

2017						
	Gross amounts of recognised financial assets/(liabilities) £m	Gross amounts of recognised financial (liabilities)/assets offset in the balance sheet £m	Net amounts of financial assets/(liabilities) presented in the balance sheet £m	Related amounts not offset in balance sheet		
				Financial instruments (Note (i)) £m	Cash collateral posted/(held) (Notes (ii) and (iii)) £m	Net amount £m
<b>Financial assets</b>						
Receivables	1,780.1	(341.1)	1,439.0	(31.1)	3.0	1,410.9
Derivative financial instruments	419.0	(247.4)	171.6	(34.0)	(44.0)	93.6
<b>Financial liabilities</b>						
Payables	(1,655.2)	341.1	(1,314.1)	31.1	(3.0)	(1,286.0)
Derivative financial instruments	(316.8)	247.4	(69.4)	34.0	–	(35.4)
2016 Restated*						
	Gross amounts of recognised financial assets/(liabilities) £m	Gross amounts of recognised financial (liabilities)/assets offset in the balance sheet £m	Net amounts of financial assets/(liabilities) presented in the balance sheet £m	Related amounts not offset in balance sheet		
				Financial instruments (Note (i)) £m	Cash collateral (held)/posted (Notes (ii) and (iii)) £m	Net amount £m
<b>Financial assets</b>						
Receivables	1,935.9	(392.6)	1,543.3	(32.4)	(4.8)	1,506.1
Derivative financial instruments	814.5	(513.0)	301.5	(73.4)	(50.3)	177.8
<b>Financial liabilities</b>						
Payables	(1,888.8)	392.6	(1,496.2)	32.4	4.8	(1,459.0)
Derivative financial instruments	(677.6)	513.0	(164.6)	73.4	–	(91.2)

\* Comparative figures have been restated (refer to Note 2).

- (i) Certain contracts for derivatives, receivables, and payables in relation to the purchase of gas do not currently meet the offsetting criteria within IAS 32 'Financial Instruments: Presentation' ("IAS 32"), however in the event of default would be required to be offset per the requirements of the contract. The above balances show the effect on the group if these contracts were also offset. Due to the nature of certain contracts, it is not possible to split accurately the effect of offsetting these balances across the derivatives, receivables and payables categories. For presentational purposes the impact has been allocated to receivables and payables as appropriate.
- (ii) 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 collateral support agreements with derivative counterparties to manage its credit exposure. All collateral is settled in cash. 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 2017, the value of letters of credit held amounted to £27.0 million (2016 £44.0 million) and letters of credit posted amounted to £252.5 million (2016 £188.2 million).
- (iii) At 31 December 2017 the group held cash collateral of £4.4 million (2016 £14.9 million) in respect of receivables, of which all (2016 all) can be offset against financial assets. At 31 December 2017 the group also posted cash collateral of £7.4 million (2016 £14.1 million) in respect of payables, of which £7.4 million (2016 £10.1 million) can be offset against financial liabilities.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 12 TRADE AND OTHER RECEIVABLES

	Notes	2017 £m	2016 Restated* £m
<b>Current receivables:</b>			
Receivables due from Iberdrola group companies – trade		8.6	10.1
Receivables due from Iberdrola group companies – loans	(a)	565.7	677.7
Receivables due from Iberdrola group companies – interest		9.6	9.5
Receivables due from jointly controlled entities – trade		1.4	1.2
Receivables due from jointly controlled entities – other		3.9	0.4
Trade receivables and accrued income	(b), (c), (d), (e)	810.7	806.5
Prepayments		59.6	59.8
Other tax receivables		18.4	18.2
		<b>1,477.9</b>	<b>1,583.4</b>
<b>Non-current receivables:</b>			
Prepayments		14.1	36.3
Other receivables	(f)	39.1	37.9
		<b>53.2</b>	<b>74.2</b>

\* Comparative figures have been restated (refer to Note 2).

- (a) Current loans receivable due from group companies are receivable on demand with interest linked to the Bank of England base rate. A 1% increase in the base rate would result in a £5.7 million increase in full year interest income.
- (b) Trade receivables are stated net of a provision for impairment of doubtful debts of £125.8 million (2016 £120.5 million). Trade receivables are assumed to approximate to 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 of change in bad debt for the year to 31 December 2017 is £59.3 million (2016 £81.5 million).
- (c) Included within Trade receivables and accrued income is billed revenue relating to the group's retail customers of £466.5 million (2016 £412.8 million) and unbilled revenue relating to the group's retail customers of £116.6 million (2016 £80.5 million).
- (d) Certain trade receivables and payables are presented net on the balance sheet when the offsetting criteria under IAS 32 are met (refer to Note 3G.5). A reconciliation between the gross and net position is provided in Note 11(c).
- (e) 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 receivables represents the maximum exposure to credit risk.
- (f) This balance represents other receivables recognised as part of a contractual renegotiation.
- (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:

	2017 £m	2016 £m
At beginning of year	120.5	94.4
Receivables written off during the year as uncollectible	(54.0)	(55.4)
Provision for receivables impairment	59.3	81.5
<b>At end of year</b>	<b>125.8</b>	<b>120.5</b>

- (i) The creation and release of the provision for impaired receivables has been included in Depreciation and amortisation charge, allowances and provisions in the consolidated income statement (refer to Note 27).
- (ii) The provision for impaired receivables mainly relates to retail customers where a low likelihood of collection has been assessed.
- (iii) At 31 December 2017, trade receivables of £68.8 million (2016 £77.2 million) that would otherwise be past due or impaired were renegotiated. These mainly relate to retail customers who, subsequent to defaulting on original payment terms, have made new arrangements to pay amounts owed.

## 13 INVENTORIES

	Notes	2017 £m	2016 Restated* £m
Fuel stocks		10.6	8.8
Emissions allowances		13.6	24.0
ROCs and LECs		234.3	143.4
Other inventories	(a)	193.6	51.3
	(b)	<b>452.1</b>	<b>227.5</b>

\* Comparative figures have been restated (refer to Note 2).

- (a) Other inventories principally represents a transmission asset which will be sold to an offshore transmission operator once it has been completed.
- (b) Inventories with a value of £419.2 million (2016 £413.8 million as restated) were recognised as an expense during the year.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 14 SHARE CAPITAL

	Note	2017 £m	2016 £m
<b>Allotted, called up and fully paid shares:</b>			
4,383,983,102 ordinary shares of 50p each (2016 1,743,983,102)	(a)	2,192.0	872.0

- (a) On 5 October 2017, the company issued 2,640,000,000 ordinary shares of 50p each, to its immediate parent, Scottish Power Limited, for a total consideration of £1,320.0 million.

## 15 ANALYSIS OF MOVEMENTS IN EQUITY ATTRIBUTABLE TO EQUITY HOLDER OF SCOTTISH POWER UK PLC

	Share capital (Note (a)) £m	Share premium (Note (b)) £m	Hedge reserve (Note (c)) £m	Translation reserve (Note (d)) £m	Other reserves (Note (e)) £m	Retained earnings (Note (f)) £m	Total £m
At 1 January 2016	872.0	398.2	(48.7)	(0.6)	14.0	2,941.9	4,176.8
Profit for the year attributable to equity holder of Scottish Power UK plc	-	-	-	-	-	580.9	580.9
Changes in the value of cash flow hedges	-	-	158.6	-	-	-	158.6
Actuarial losses on retirement benefits	-	-	-	-	-	(251.4)	(251.4)
Tax relating to cash flow hedges	-	-	(30.7)	-	-	-	(30.7)
Tax relating to actuarial losses on retirement benefits	-	-	-	-	-	42.1	42.1
Exchange movement on translation of overseas results and net assets	-	-	-	0.9	-	-	0.9
Dividends	-	-	-	-	-	(663.0)	(663.0)
At 1 January 2017	872.0	398.2	79.2	0.3	14.0	2,650.5	4,014.2
Profit for the year attributable to equity holder of Scottish Power UK plc	-	-	-	-	-	425.9	425.9
Share capital issued	1,320.0	-	-	-	-	-	1,320.0
Changes in the value of cash flow hedges	-	-	8.9	-	-	-	8.9
Actuarial losses on retirement benefits	-	-	-	-	-	(222.9)	(222.9)
Tax relating to cash flow hedges	-	-	(1.7)	-	-	-	(1.7)
Tax relating to actuarial losses on retirement benefits	-	-	-	-	-	36.4	36.4
Exchange movement on translation of overseas results and net assets	-	-	-	0.2	-	-	0.2
Group restructuring	-	-	-	(0.5)	-	-	(0.5)
Dividends	-	-	-	-	-	(300.0)	(300.0)
At 31 December 2017	2,192.0	398.2	86.4	-	14.0	2,589.9	5,280.5

- (a) On 5 October 2017, the company issued 2,640,000,000 ordinary shares of 50p each, to its immediate parent, Scottish Power Limited, for a total consideration of £1,320.0 million.

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

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

- (d) The translation reserve represents the accumulated exchange differences on the translation of the results and net assets of foreign subsidiaries.

- (e) Other reserves at 31 December 2017 comprises a revaluation reserve of £5.8 million (2016 £5.8 million) and a capital redemption reserve of £8.2 million (2016 £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 represents the cumulative nominal value of shares repurchased and cancelled by the company.

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

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 15 ANALYSIS OF MOVEMENTS IN EQUITY ATTRIBUTABLE TO EQUITY HOLDER OF SCOTTISH POWER UK PLC *continued*

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

	Commodity hedges £m	Foreign exchange rate hedges £m	Gross value of hedges £m	Tax effect £m	Total £m
<b>Cash flow hedges</b>					
At 1 January 2016	(52.0)	(9.1)	(61.1)	12.4	(48.7)
Effective cash flow hedges recognised	3.1	90.4	93.5	(18.7)	74.8
De-designated cash flow hedges	0.6	(0.1)	0.5	(0.1)	0.4
Removed from equity and recognised in income statement	72.7	(1.7)	71.0	(14.2)	56.8
Removed from equity and recognised in carrying amount of hedged items	1.0	(7.4)	(6.4)	1.3	(5.1)
Change in tax rates	–	–	–	1.0	1.0
At 1 January 2017	25.4	72.1	97.5	(18.3)	79.2
Effective cash flow hedges recognised	23.8	1.3	25.1	(4.8)	20.3
De-designated cash flow hedges	0.2	–	0.2	–	0.2
Removed from equity and recognised in income statement	5.4	(0.5)	4.9	(0.9)	4.0
Removed from equity and recognised in carrying amount of hedged items	–	(21.3)	(21.3)	4.0	(17.3)
<b>At 31 December 2017</b>	<b>54.8</b>	<b>51.6</b>	<b>106.4</b>	<b>(20.0)</b>	<b>86.4</b>

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

	2017 £m	2016 £m
Less than 1 year	40.3	18.0
1-2 years	35.4	27.1
2-3 years	10.1	25.9
3-4 years	0.6	7.3
4-5 years	–	0.9
	<b>86.4</b>	<b>79.2</b>

## 16 NON-CONTROLLING INTERESTS

	£m
At 1 January 2016	0.5
Net profit attributable to non-controlling interests	0.1
At 1 January 2017	0.6
Net profit attributable to non-controlling interests	0.2
Group restructuring	0.1
<b>At 31 December 2017</b>	<b>0.9</b>

## 17 DEFERRED INCOME

	At 1 January 2016 £m	Receivable during year £m	Released to income statement £m	At 31 December 2016 £m
Year ended 31 December 2016				
Capital grants	0.5	–	(0.1)	0.4
Transfer of assets from customers	1,007.1	132.0	(32.2)	1,106.9
Emissions allowances allocated	–	0.1	(0.1)	–
Total deferred income	1,007.6	132.1	(32.4)	1,107.3

	At 1 January 2017 £m	Receivable during year £m	Released to income statement £m	Disposals £m	At 31 December 2017 £m
Year ended 31 December 2017					
Capital grants	0.4	–	–	–	0.4
Transfer of assets from customers	1,106.9	115.3	(35.3)	(3.7)	1,183.2
Emissions allowances allocated	–	0.1	(0.1)	–	–
Total deferred income	1,107.3	115.4	(35.4)	(3.7)	1,183.6

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 18 RETIREMENT BENEFIT OBLIGATIONS

### (a) Analysis of balance

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

	2017 £m	2016 £m
Non-current liabilities	564.8	442.5

### (b) Group pension arrangements

The group 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 2015)	Agreement of Trustees and group following actuarial valuation (last valuation: 31 March 2015)	Defined
Current actual group contributions	48% of salary	45% of salary	Service-related, 6% to 14% of salary
Special contributions during year ended 31 December 2017	£50.0 million	£39.0 million	None
Special contributions planned for year ending 31 December 2018	£52.0 million	£40.5 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

\* A number of members of the Stakeholder Pension Plan were entitled to defined benefits for future service upon achieving ten years of membership. The group has withdrawn this option and therefore there is no benefit accrual for Stakeholder members.

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.

#### Group pension scheme governance

As described in the table above, the group operates two defined benefit pension schemes. Active members continue to accrue benefits in the schemes, which are based on final pensionable salary. The two schemes are however closed to new entrants. The schemes provide benefits which are based on final pensionable salary.

The schemes are approved by HMRC and subject to standard UK pensions and tax law. The defined benefit schemes are subject to the scheme funding requirements as set out in section 224 of the Pensions Act 2004. In accordance with the scheme funding requirements, an actuarial funding valuation is carried out at least triennially to determine the appropriate level of ongoing contributions for both future service and a recovery plan in respect of any deficit at the valuation date. These actuarial valuations will be based on assumptions agreed between the Trustees and the group. The assumptions used to calculate liabilities (or technical provisions) in a triennial funding valuation may differ from those used in IAS 19 accounting. The Trustees are required to set assumptions prudently, whereas IAS 19 assumptions are set with regard to the group's best estimates. Additionally, the discount rate used to value technical provisions will take into account the scheme investment strategy rather than being based on the yield on AA corporate bonds as required under IAS 19. The most recent completed actuarial valuation was as at the effective date of 31 March 2015. The valuations for SPPS and Manweb were agreed in December 2016. The new recovery plans and schedules of contributions came in to effect from 1 January 2017. Company contribution rates increased from 31% to 48% for SPPS and from 30.1% to 45% for Manweb. In addition to the deficit contributions expected to be paid in 2018 (as shown in the above table), £21 million and £7 million was paid in January 2017 for SPPS and Manweb respectively to cover backdated future service contributions.

In accordance with UK trust and pensions law, the defined benefit pension schemes are governed by their respective Board of Trustees. Although the group meets the financial cost of running the schemes, the Trustees are responsible for the management and governance of the schemes and have a duty to act in the best interests of the members.

The strategic management of the assets is the responsibility of the Trustees acting on expert advice. The Trustees take advice from the schemes' actuaries and investment advisers with a view to investing the schemes' assets in a manner that is appropriate to the nature and duration of the expected future retirement and death benefits payable from the schemes. In consultation with the group, the Trustees have set out a target investment strategy for the schemes of 49% matching and 51% growth assets. In terms of the matching portfolio, the schemes utilise a Liability Driven Investment ("LDI") strategy. The aim of the LDI portfolio is to invest in a range of assets (mostly bonds) which broadly match the expected future benefit payments from the schemes.

In addition, the Trustees of the Scottish Power Pension Scheme and the Trustees of the Manweb Group of Electricity Supply Pension Scheme have implemented longevity swaps in December 2014 and July 2016 respectively. For further details, please see the 'Mortality risk' section that follows.

Following the decision by the UK to exit the EU, there has been significant market volatility. Despite the Bank of England's recent decision to increase base rates, long-term yields on both government and corporate bonds continue to remain low and liabilities are still at a high levels. Negotiations between the UK and the EU continue ahead of the exit date of March 2019. The Trustees continue to monitor how decisions impact on the schemes from an investment and legal perspective based on expert advice.

#### Risk management

The defined benefit schemes expose the group to actuarial risks and details of the specific risks and how they are managed are described below.

**Investment (market) risk:** there is a risk relating to changes in the value of the portfolio due to movements in the market value of the assets. To the extent that there is a mismatch between the investment strategy and the overall level and profile of the liabilities this can lead to volatility in the funding level and as the portfolio matures there is a risk of not being able to reinvest assets at the assumed rates. The Trustees utilise an LDI strategy which aims to invest 49% of the assets in matching LDIs such as bonds, which broadly match the nature and profile of the future expected benefit payments from the scheme. The Trustees have further diversified the market risk in the growth portfolio across multiple asset types, such as equities, property, diversified growth funds, infrastructure, private and mezzanine debt, and multi-asset credit. Through diversification, the specific risk associated with individual investments is mostly mitigated and expected volatility of returns is reduced. In addition, the Trustees review the investment strategy on a regular basis to ensure that it remains appropriate and in particular in response to legislative changes, a material change in the schemes' funding levels or changes in the attitude to risk of the Trustees or group.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 18 RETIREMENT BENEFIT OBLIGATIONS *continued*

### (b) Group pension arrangements *continued*

**Mortality risk:** the assumptions adopted by the group make allowance for future improvements in life expectancy. There is a risk that life expectancy improves faster than assumed and that benefits are paid for longer than expected, thereby increasing the cost of the schemes. The group and the Trustees regularly review the actual scheme mortality experience to minimise the risk of using an inappropriate assumption. In general, the Trustees will also use prudent assumptions when deriving the triennial actuarial valuation basis used for funding requirements and this will help to manage the risk.

In December 2014, the Trustees of SPPS implemented a longevity swap in respect of the current pensioners. The swap removes the previously unhedged longevity risk for the current pensioners (who constitute approximately 50% of the total liability of the scheme) and their contingent spouses by hedging the risk of members covered by the contract living longer than expected. The swap is an insurance contract between SPPS and the counterparty insurer. Counterparty risk is mitigated by both SPPS and the counterparty posting collateral to the other party on a daily basis to account for market movements in the value of the derivatives held.

In July 2016, the Trustees of Manweb also implemented a longevity swap in respect of the current pensioners. The swap removes the previously unhedged longevity risk for the current pensioners (who constitute approximately 50% of the total liability of the scheme) and their contingent spouses by hedging the risk of members covered by the contract living longer than expected. The swap is an insurance contract between Manweb and the counterparty insurer. Counterparty risk is mitigated by both Manweb and the counterparty posting collateral to the other party on a daily basis to account for market movements in the value of the derivatives held.

**Interest rate risk:** a fall in the yield on government bonds increases both the liabilities and assets of the schemes. To the extent that the assets do not fully match the nature and duration of the liabilities, this could lead to a worsening in the funding position of the schemes. The Trustees currently target 49% of the schemes' investments in LDI which include matching assets such as fixed interest bonds. The interest rate hedging strategy adopted within the LDI portfolio provides partial protection against the impact of changes in yields. Around 55% of the interest rate risk is currently hedged on a technical provision basis. Under the de-risking framework agreed between the group and the Trustees, the level of interest rate hedging will be increased when market conditions are deemed favourable. As the level of the hedging increases, funding level volatility will be further reduced.

**Inflation rate risk:** the majority of the schemes' liabilities increase in line with inflation, subject to relevant caps and collars. To the extent that inflation is higher than expected, this will increase the liabilities of the schemes. The schemes' target investment strategy is to invest 49% of the portfolio in LDI investments which will include bonds which are also linked to inflation. The inflation hedging strategy adopted within the LDI portfolio provides partial protection against the impact of changes in inflation. Around 65% of the interest rate risk is currently hedged on a technical provision basis. Under the de-risking framework agreed between the group and the Trustees, the level of interest rate hedging will be increased when market conditions are deemed favourable. As the level of the hedging increases, funding level volatility will be further reduced.

Each of the pension schemes is invested in an appropriately diversified range of assets. The broad proportion 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.

	2017	2016
Equities	15%	21%
Infrastructure	3%	3%
Liability driven investment	49%	55%
Property	4%	4%
Mezzanine debt	5%	5%
Diversified growth funds	16%	12%
Multi-asset credit	8%	–
Total	100%	100%

**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 £5.8 million as at 31 December 2017 (2016 £6.2 million) for the benefit promises which will ultimately be paid by the group.

In addition to the defined benefit schemes described above, the group also operates a defined contribution scheme which is open to new entrants. This scheme is a contract based arrangement to which both the group and the employee contribute.

### (c) Pensions – defined contribution scheme

The charge for the year ended 31 December 2017 in respect of the Stakeholder Pension Plan is £8.4 million (2016 £6.8 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 2017 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

	2017 £m	2016 £m
Present value of funded obligations	(5,477.9)	(5,324.2)
Fair value of scheme assets	4,918.9	4,887.9
<b>Net liability of funded plans</b>	<b>(559.0)</b>	<b>(436.3)</b>
Present value of unfunded obligations	(5.8)	(6.2)
<b>Net liability</b>	<b>(564.8)</b>	<b>(442.5)</b>
Amounts in the balance sheet:		
Non-current liabilities	(564.8)	(442.5)
<b>Net liability</b>	<b>(564.8)</b>	<b>(442.5)</b>

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 18 RETIREMENT BENEFIT OBLIGATIONS *continued*

### (d) Pensions – defined benefit schemes *continued*

(ii) The amounts recognised are as follows:

	2017 £m	2016 £m
Current service cost	58.4	52.3
Past service cost	31.1	14.8
Net interest cost on defined benefit obligation/scheme assets	9.4	6.8
Administration expenses	2.7	2.5
<b>Total income statement charge</b>	<b>101.6</b>	<b>76.4</b>
<b>Actual return on scheme assets</b>	<b>225.9</b>	<b>616.9</b>
<b>Net actuarial losses recognised in the consolidated statement of comprehensive income</b>	<b>(222.9)</b>	<b>(251.4)</b>

Past service costs in 2017 primarily include the pension costs recognised following the announcement of a group wide restructuring programme during 2017. In 2016 these costs related to a restructuring programme within the Energy Retail business function.

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

	2017 £m	2016 £m
Defined benefit obligation at beginning of year	(5,330.4)	(4,642.2)
Current service cost	(58.4)	(52.3)
Interest on obligation	(149.9)	(171.6)
Scheme members' contributions	(7.5)	(8.6)
Past service costs	(31.1)	(14.8)
Actuarial gains/(losses):		
Actuarial gains arising from changes in demographic assumptions	161.1	30.8
Actuarial losses arising from changes in financial assumptions	(510.0)	(719.7)
Actuarial gains/(losses) arising from changes of the scheme experience different to that assumed	40.6	(14.6)
Benefits paid	401.9	262.6
<b>Defined benefit obligation at end of year</b>	<b>(5,483.7)</b>	<b>(5,330.4)</b>
Analysis of defined benefit obligation		
Plans that are wholly or partly funded	(5,477.9)	(5,324.2)
Plans that are wholly unfunded	(5.8)	(6.2)
<b>Total</b>	<b>(5,483.7)</b>	<b>(5,330.4)</b>

The defined benefit obligations for SPPS are 32% (2016 34%) in respect of active scheme participants, 16% (2016 14%) in respect of deferred scheme participants and 52% (2016 52%) in respect of retirees. The weighted average duration of the defined benefit obligation as at 31 December 2017 is 21 years.

The defined benefit obligations for Manweb are 33% (2016 38%) in respect of active scheme participants, 10% (2016 7%) in respect of deferred scheme participants and 57% (2016 55%) in respect of retirees. The weighted average duration of the defined benefit obligation as at 31 December 2017 is 19 years.

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

	2017 £m	2016 £m
Fair value of scheme assets at beginning of year	4,887.9	4,377.8
Interest income on scheme assets	140.5	164.8
Return on assets in excess of interest income	85.4	452.1
Employer contributions	202.2	149.7
Scheme members' contributions	7.5	8.6
Administration expenses	(2.7)	(2.5)
Benefits paid	(401.9)	(262.6)
<b>Fair value of scheme assets at end of year</b>	<b>4,918.9</b>	<b>4,887.9</b>

### (e) Actuarial assumptions

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

	2017	2016
Rate of increase in salaries	3.7% p.a.	3.5% p.a.
Rate of increase in deferred pensions	3.2% p.a.	3.0% p.a.
Rate of increase to pensions in payment	3.1% p.a.	2.9% p.a.
Discount rate	2.6% p.a.	2.9% p.a.
Inflation assumption	3.2% p.a.	3.0% p.a.

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

Member age 63 (current life expectancy)	2017	2016
Male	24.8	25.6
Female	25.9	26.7
Member age 45 (life expectancy at age 63)		
Male	26.5	27.7
Female	27.7	28.9

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

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## 18 RETIREMENT BENEFIT OBLIGATIONS *continued*

### (e) Actuarial assumptions *continued*

(iii) The sensitivity analysis below has been calculated by varying the critical actuarial assumption whilst keeping all other assumptions constant. Liabilities are calculated using the same method and membership data as that used to derive the defined benefit obligation. As well as impacting on salary growth, a change in inflation also impacts on other inflation linked assumptions such as increases to deferred pensions and pensions in payment. This sensitivity applies to the defined benefit obligation only and not to the net defined benefit pension liability in its entirety, the measurement of which is driven by a number of factors including, in addition to the assumptions below, the fair value of scheme assets.

	Increase/(decrease) in defined benefit obligation	
	2017 £m	2016 £m
<b>Sensitivity analysis of critical actuarial assumptions</b>		
Rates of increase in inflation and salary growth		
Increase by 0.1%	103.3	99.8
Decrease by 0.1%	(100.5)	(27.1)
Discount rate		
Increase by 0.25%	(257.4)	(248.4)
Decrease by 0.25%	277.2	267.7
Assumed life expectancy		
Increase mortality by one additional year	204.7	181.6

(iv) 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.

(v) The following table provides information on the composition and fair value of plan assets of the SPPS and Manweb pension schemes:

SPPS Scheme	2017					2016				
	Level 1	Level 2	Level 3	Total	Plan asset allocation	Level 1	Level 2	Level 3	Total	Plan asset allocation
	£m	£m	£m	£m	%	£m	£m	£m	£m	%
Equities	704.3	–	–	704.3	19.1%	848.9	–	–	848.9	23.3%
Infrastructure	–	–	113.6	113.6	3.1%	–	–	108.4	108.4	3.0%
Liability driven instrument	1,450.1	31.1	–	1,481.2	40.1%	1,613.5	250.4	–	1,863.9	51.0%
Property	0.4	–	193.3	193.7	5.3%	0.6	–	150.2	150.8	4.1%
Cash	216.7	–	–	216.7	5.9%	189.4	–	–	189.4	5.2%
Mezzanine debt	–	–	149.3	149.3	4.0%	–	–	128.5	128.5	3.5%
Diversified growth funds	559.1	–	–	559.1	15.2%	311.4	–	–	311.4	8.5%
Multi-asset credit	52.7	215.9	1.6	270.2	7.3%	–	–	–	–	–
BMO – Guaranteed government debt	–	–	–	–	–	50.3	–	–	50.3	1.4%
Fair value of scheme assets	2,983.3	247.0	457.8	3,688.1	100%	3,014.1	250.4	387.1	3,651.6	100%

Manweb Scheme	2017					2016				
	Level 1	Level 2	Level 3	Total	Plan asset allocation	Level 1	Level 2	Level 3	Total	Plan asset allocation
	£m	£m	£m	£m	%	£m	£m	£m	£m	%
Equities	199.0	–	–	199.0	16.2%	291.8	–	–	291.8	23.6%
Infrastructure	–	–	34.1	34.1	2.8%	–	–	32.5	32.5	2.6%
Liability driven instrument	518.6	27.2	–	545.8	44.3%	594.5	16.3	–	610.8	49.4%
Cash	88.8	–	–	88.8	7.2%	76.0	–	–	76.0	6.2%
Mezzanine/private debt	–	–	24.3	24.3	2.0%	–	–	–	–	–
Diversified growth funds	239.0	–	–	239.0	19.4%	225.2	–	–	225.2	18.2%
Multi-asset credit	28.4	70.2	1.2	99.8	8.1%	–	–	–	–	–
Fair value of scheme assets	1,073.8	97.4	59.6	1,230.8	100%	1,187.5	16.3	32.5	1,236.3	100%
Total				4,918.9					4,887.9	

The scheme assets do not include any of the group's own financial instruments, nor any property occupied by, or other assets used by, the group.

No scheme held ScottishPower or Iberdrola shares in 2017 or 2016.

The group uses the value of the variation collateral posted as the fair value of the longevity swaps for SPPS and Manweb. The amount of collateral posted is calculated and agreed between insurer and scheme custodian. The valuation takes into consideration current market conditions at the balance sheet date. This allows for the difference between the present value of cash flows allowing for actual longevity experience for the schemes and the present value of cash flows using the longevity assumptions agreed at the inception of the swaps. As at 31 December 2017, the value of the variation collateral for SPPS was (£129.4) million and the value for Manweb was (£11.5) million and these have been allowed for as a reduction to the cash value.

Under the rules of each scheme, the Trustees cannot unilaterally wind-up the schemes and the group would be able to assume gradual settlement of the liabilities over time until all members have left. Having then triggered a wind-up, any remaining surplus would revert to the group. Furthermore, the power to amend the rules of each scheme lies with the group and the Trustees cannot unilaterally improve benefits under the schemes. Therefore, the group has an unconditional right to a refund under IFRIC 14 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction' and thus there is no requirement to restrict any IAS 19 surplus, should it arise, nor to recognise any additional liabilities in respect of minimum funding requirements.

### (f) Future contributions

The group expects to contribute £160.9 million to the pension schemes in the year ending 31 December 2018, based on the agreement with scheme Trustees following the valuation at March 2015.



# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

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## 19 OTHER PROVISIONS

Year ended 31 December 2016	Notes	At 1 January 2016 Restated* £m	New provisions £m	Unwinding of discount £m	Utilised during year Restated* £m	Released during year £m	At 31 December 2016 Restated* £m
Reorganisation and restructuring	(a)	6.1	5.1	–	(4.7)	(0.5)	6.0
Decommissioning and environmental	(b)	209.2	17.7	3.6	(28.0)	(3.2)	199.3
Emissions allowances	(c)	56.2	23.7	–	(54.7)	(1.5)	23.7
ROCs and LECs	(d)	195.6	328.6	–	(264.2)	–	260.0
Onerous contracts	(e)	21.0	(6.7)	0.2	(5.5)	(0.3)	8.7
Insurance	(f)	4.1	2.3	–	(1.7)	(1.1)	3.6
Other	(g)	5.9	0.1	–	(0.3)	(0.6)	5.1
		498.1	370.8	3.8	(359.1)	(7.2)	506.4

Year ended 31 December 2017	Notes	At 1 January 2017 £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	Released during year £m	At 31 December 2017 £m
Reorganisation and restructuring	(a)	6.0	4.1	–	(4.5)	(1.1)	4.5
Decommissioning and environmental	(b)	199.3	31.2	3.2	(2.6)	(0.1)	231.0
Emissions allowances	(c)	23.7	13.4	–	(23.7)	–	13.4
ROCs and LECs	(d)	260.0	402.8	–	(337.8)	–	325.0
Onerous contracts	(e)	8.7	0.2	0.2	(1.4)	–	7.7
Insurance	(f)	3.6	1.3	–	(0.2)	(0.9)	3.8
Other	(g)	5.1	3.3	–	(1.1)	–	7.3
		506.4	456.3	3.4	(371.3)	(2.1)	592.7

Analysis of total provisions	2017 £m	2016 Restated* £m
Non-current	231.8	194.9
Current	360.9	311.5
	592.7	506.4

\* Comparative figures have been restated (refer to Note 2).

- (a) The provision for reorganisation and restructuring in 2016 related to the Energy Retail business function and was largely utilised in 2017; the remainder is expected to be utilised in 2018. The new provision for reorganisation and restructuring in 2017 relates to a group wide restructuring programme and is expected to be utilised in 2018.
- (b) The provision for decommissioning and environmental costs is the discounted future estimated costs of decommissioning the group's power plants 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 2018 and 2056.
- (c) The provision for emissions allowances represents the value of emissions allowances certificates expected to be delivered in the year ahead.
- (d) The provision for the ROCs and LECs principally represents the value of ROCs for 2017 expected to be delivered in the year ahead.
- (e) The provision for onerous contracts principally relates to various property leases. These leases will expire over the period between 2018 and 2025.
- (f) The provision for insurance principally represents the value of claims reserves. The claims are expected to be settled between 2018 and 2020.
- (g) The 'Other' category comprises provisions which are not individually sufficiently material to warrant separate disclosure.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 20 LOANS AND OTHER BORROWINGS

Analysis by instrument and maturity	Notes	Interest rate <sup>*</sup>	Maturity	2017 £m	2016 £m
Bank overdraft		Base + 1%	On demand	0.1	–
Loans with Iberdrola group companies		Base + 1%	On demand	2,469.9	3,846.0
Loans with Iberdrola group companies	(b), (c)	EURIBOR + 0.4593%	On demand	–	22.2
Loans with Iberdrola group companies	(b), (c)	EUR 3 month + 1.1892%	On demand	–	51.3
£200 million euro-sterling bond	(d)	8.375%	20 February 2017	–	200.0
Loan with Avel Vor Energie Eolienne	(b)	EUR 12 month + 1.11%	31 January 2018	–	10.6
Collateral		LIBOR	17 June 2018	44.0	50.3
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
Loans with Iberdrola group companies	(b), (c)	EUR 3 month + 0.785%	1 May 2020	–	255.4
Loans with Iberdrola group companies	(b)	5.135%	1 August 2020	–	23.8
Loans with Iberdrola group companies	(b)	1.262%	2 November 2020	–	85.1
£300 million medium-term note	(e)	5.9%	22 February 2021	297.9	297.2
Loans with Iberdrola group companies	(f)	EURIBOR + 1.025%	28 March 2022	85.4	100.0
Loans with Iberdrola group companies	(b)	2.25%	3 April 2023	–	170.3
£250 million euro-sterling bond	(d), (g)	6.75%	29 May 2023	249.1	248.9
£175 million inflation linked bond	(e)	3.494% x RPI	13 October 2024	283.3	273.6
£350 million euro-sterling bond	(d), (h)	5.875%	17 July 2026	347.5	347.2
£350 million euro-sterling bond	(d), (i)	4.875%	20 September 2027	346.8	346.5
Loans with Iberdrola group companies		2.66%	20 December 2027	100.0	–
Loans with Iberdrola group companies		3.05%	20 December 2027	900.0	–
10 billion JPY loan	(j)	4.6%	27 July 2029	93.8	104.6
£50 million medium-term note	(e)	5.75%	9 December 2039	50.0	50.0
£100 million medium-term note	(e)	6.375%	31 May 2041	100.0	100.0
				<b>5,667.8</b>	<b>6,883.0</b>

<sup>\*</sup> 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	2017 £m	2016 £m
Non-current		2,986.4	2,698.1
Current	(a)	2,681.4	4,184.9
		<b>5,667.8</b>	<b>6,883.0</b>

- (a) Current borrowings comprise loans with Iberdrola group companies repayable on demand, the short-term element of the EURIBOR 2022 loan with Iberdrola (refer to footnote (f) below) 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, which totalled (£1.8) million (2016 £(3.3) million).
- (b) These loans related to the group's operations in France and Germany which were disposed of in 2017 (refer to Note 36).
- (c) These loans have the interest rates reset at pre-determined dates, this includes the ability to adjust the margin rate as deemed appropriate by both parties.
- (d) These bonds contain a "Loss of licences" covenant that will require repayment of the outstanding amount should the group lose all of their electricity licences (distribution, transmission and supply licences).
- (e) Scottish Power UK plc ("SPUK") and Scottish Power Limited have an established joint US\$7 billion euro medium-term note programme. Scottish Power Limited has not issued under the programme. SPUK has in issue various notes in Sterling which can be redeemed by SPUK with 30 to 90 days' notice in case of unfavourable and unavoidable changes in the UK tax laws impacting on the note payments.
- (f) The EURIBOR loan with Iberdrola that is due to mature in March 2022 has a schedule of repayments which commenced in 2014. The repayment of £19.2 million due in 2018 (2016 £18.4 million due in 2017) is classified as current in the above analysis.
- (g) The euro-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.
- (h) 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 Fiscal Agent) giving 30 to 60 days' notice.
- (i) The £350 million euro-sterling bond will be redeemed at its principal 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 Fiscal Agent) giving 30 to 60 days' notice.
- (j) 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.
- (k) The group has no undrawn committed borrowing facilities at 31 December 2017 (2016 nil).

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

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## 20 LOANS AND OTHER BORROWINGS *continued*

(i) Reconciliation of movements of liabilities to cash flows arising from financing activities

	Liabilities			Total £m
	Loans and other borrowings (Current) £m	Loans and other borrowings (Non-current) £m	Interest payable (Current) (Note (ii)) £m	
<b>At 1 January 2017</b>	<b>4,184.9</b>	<b>2,698.1</b>	<b>109.4</b>	<b>6,992.4</b>
(Decrease)/increase in amounts due to Iberdrola group companies	(1,147.3)	989.7	–	(157.6)
(Repayments of)/cash inflows from borrowings	(206.3)	1.1	–	(205.2)
Interest paid	–	–	(169.7)	(169.7)
<b>Total movements from financing cash flows</b>	<b>(1,353.6)</b>	<b>990.8</b>	<b>(169.7)</b>	<b>(532.5)</b>
<b>Movements arising from group restructuring</b>	<b>(311.1)</b>	<b>(574.8)</b>	<b>(4.0)</b>	<b>(889.9)</b>
<b>Foreign exchange movement</b>	<b>8.8</b>	<b>28.4</b>	<b>0.2</b>	<b>37.4</b>
Fair value and other non-cash movements	2.4	(6.1)	(29.6)	(33.3)
Other movements	150.0	(150.0)	191.1	191.1
<b>Total liability-related other movements</b>	<b>(149.9)</b>	<b>(702.5)</b>	<b>157.7</b>	<b>(694.7)</b>
<b>At 31 December 2017</b>	<b>2,681.4</b>	<b>2,986.4</b>	<b>97.4</b>	<b>5,765.2</b>

(i) External interest payable of £37.9 million (2016 £52.3 million) and internal interest payable of £59.5 million (2016 £57.1 million) are included within Trade and other payables (refer to Note 23).

## 21 DERIVATIVE FINANCIAL INSTRUMENTS

Analysis of derivative financial instruments – carrying value

	Note	2017				2016			
		Assets		Liabilities		Assets		Liabilities	
		Current £m	Non- current £m	Current £m	Non- current £m	Current £m	Non- current £m	Current £m	Non- current £m
<b>Hedging derivatives:</b>									
Exchange rate hedges									
Fair value hedge – Currency swap		1.0	43.1	–	–	1.1	53.9	–	–
Cash flow hedge – Foreign exchange rate		7.2	1.0	(5.3)	–	41.3	5.0	(13.9)	(0.4)
Commodity hedge – Cash flow hedge		46.2	20.5	(10.6)	(1.1)	48.8	36.7	(37.0)	(2.2)
<b>Non-hedging derivatives:</b>									
Exchange rate derivatives – Foreign exchange rate		–	–	–	–	2.3	–	(2.0)	–
Commodity derivatives		298.3	1.7	(298.4)	(1.4)	618.6	6.8	(614.9)	(7.2)
<b>Total gross derivatives</b>		<b>352.7</b>	<b>66.3</b>	<b>(314.3)</b>	<b>(2.5)</b>	<b>712.1</b>	<b>102.4</b>	<b>(667.8)</b>	<b>(9.8)</b>
Impact of netting	(a)	(245.4)	(2.0)	245.4	2.0	(506.3)	(6.7)	506.3	6.7
<b>Total net derivatives in balance sheet</b>		<b>107.3</b>	<b>64.3</b>	<b>(68.9)</b>	<b>(0.5)</b>	<b>205.8</b>	<b>95.7</b>	<b>(161.5)</b>	<b>(3.1)</b>

(a) Certain derivative financial instruments are presented net on the balance sheet. A reconciliation between the gross and net position is provided in Note 11(c).

## 22 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	2017 £m	2016 £m
<b>Operating derivatives:</b>			
Effect of operating derivative instruments	(a)	(23.9)	54.1
<b>Financing derivatives:</b>			
Effect of foreign exchange rate derivatives	(a)	(0.8)	(1.6)
<b>Fair value hedges:</b>			
Movements in the fair value of hedging instruments		(6.8)	7.8
Movements in the fair value of hedged item		6.8	(7.8)
<b>Effect of fair value hedges</b>		<b>–</b>	<b>–</b>
<b>Cash flow hedges – amounts released from equity:</b>			
Commodities		(5.4)	(72.7)
Foreign exchange rate derivatives		0.5	1.7
<b>Effect of cash flow hedges</b>	(b)	<b>(4.9)</b>	<b>(71.0)</b>
<b>Total</b>	(c)	<b>(29.6)</b>	<b>(18.5)</b>

(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.

(c) The net effect of hedging and derivative financial instruments with Iberdrola group companies on the income statement for the year ended 31 December 2017 was £(10.7) million (2016 £45.7 million).

## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 23 TRADE AND OTHER PAYABLES

	Notes	2017 £m	2016 Restated* £m
<b>Current trade and other payables:</b>			
Payables due to Iberdrola group companies – trade		8.8	37.4
Payables due to Iberdrola group companies – capital		2.1	41.5
Payables due to Iberdrola group companies – interest		59.5	57.1
Payables due to jointly controlled entities – trade		3.4	6.6
Trade payables	(a), (b)	535.7	574.3
Other tax payables		68.6	70.6
Payments received on account		136.7	152.3
Capital payables and accruals		542.7	580.3
Other payables		157.4	194.4
		<b>1,514.9</b>	<b>1,714.5</b>
<b>Non-current other payables:</b>			
Payments received on account		29.2	30.6
Other payables		4.5	4.6
		<b>33.7</b>	<b>35.2</b>

\* Comparative figures have been restated (refer to Note 2).

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

(b) Certain trade payables and receivables are presented net on the balance sheet when offsetting criteria under IAS 32 are met (refer to Note 3G.5). A reconciliation between the gross and net position is provided at Note 11(c).

### 24 DEFERRED TAX

Deferred tax provided in the Accounts is as follows:

Note	Property, plant and equipment £m	Derivative financial instruments £m	Retirement benefits £m	Intangible assets £m	Other temporary differences £m	Total £m
At 1 January 2016	722.4	(22.6)	(52.9)	51.5	(8.4)	690.0
Charge/(credit) to income statement	60.1	16.1	12.9	(51.5)	0.6	38.2
Recorded in the statement of comprehensive income	–	30.7	(42.1)	–	–	(11.4)
Exchange	–	–	–	–	(0.5)	(0.5)
At 1 January 2017	782.5	24.2	(82.1)	–	(8.3)	716.3
Charge/(credit) to income statement	37.4	(3.9)	19.2	–	(1.7)	51.0
Group restructuring	(c)	–	–	–	6.0	6.0
Recorded in the statement of comprehensive income	–	1.7	(36.4)	–	–	(34.7)
Exchange	–	–	–	–	(0.4)	(0.4)
At 31 December 2017	819.9	22.0	(99.3)	–	(4.4)	738.2

Deferred tax presented in the Accounts is as follows:

Note	2017 £m	2016 £m
Non-current assets	(d)	–
Non-current liabilities		(721.5)
	<b>(738.2)</b>	<b>(716.3)</b>

(a) At 31 December 2017, the group had unutilised capital losses of £26.0 million (2016 £22.3 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) Legislation has been enacted to reduce the rate of UK Corporation Tax to 17% on 1 April 2020. This reduces the tax rates expected to apply when temporary differences reverse and impacts the deferred tax charge.

(c) Group restructuring of £6.0 million in 2017 relates to the disposal of the group's operations in France and Germany (refer to Note 36).

(d) The deferred tax asset in 2016 relates to losses from the group's operations in Germany which were disposed of on 1 August 2017 (refer to Note 36).

### 25 EMPLOYEE INFORMATION

#### (a) Staff costs

Note	2017 £m	2016 £m
Wages and salaries	281.0	273.2
Social security costs	30.1	28.1
Pension and other costs	(i)	93.8
<b>Total staff costs</b>	<b>429.1</b>	<b>395.1</b>
Less: capitalised staff costs	(142.6)	(132.6)
<b>Charged to the income statement</b>	<b>286.5</b>	<b>262.5</b>

(i) Pension and other costs in 2017 includes £38.1 million of costs for a group wide restructuring programme. In 2016 this included £19.7 million costs for a restructuring programme within the Energy Retail business function.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 25 EMPLOYEE INFORMATION *continued*

### (b) Employee numbers

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

	Year end 2017	Average 2017	Year end 2016	Average 2016
Energy Networks	3,014	2,876	2,857	2,912
Energy Wholesale and Retail	2,154	2,289	2,405	2,498
Renewables	367	304	312	292
Corporate	531	503	499	503
<b>Total</b>	<b>6,066</b>	<b>5,972</b>	<b>6,073</b>	<b>6,205</b>

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

	Year end 2017	Average 2017	Year end 2016	Average 2016
<b>Total</b>	<b>5,864</b>	<b>5,799</b>	<b>5,861</b>	<b>6,004</b>

## 26 TAXES OTHER THAN INCOME TAX

	Note	2017 £m	2016 £m
Property taxes		121.1	115.9
Business taxes		–	0.4
Other taxes	(a)	102.2	76.9
		<b>223.3</b>	<b>193.2</b>

(a) Other taxes mainly comprise obligations specific to the energy industry, which in both years principally comprised ECO and WHD.

## 27 DEPRECIATION AND AMORTISATION CHARGE, ALLOWANCES AND PROVISIONS

	Note	2017 £m	2016 £m
Property, plant and equipment depreciation charge		436.9	413.8
Intangible asset amortisation		60.2	60.6
Charges and provisions, allowances and impairment of assets	(a)	73.8	82.1
		<b>570.9</b>	<b>556.5</b>

(a) Charges and provisions, allowances and impairment of assets includes a charge of £59.3 million (2016 £81.5 million) for the impairment of receivables (refer to Note 12 (h)).

## 28 FINANCE INCOME

	2017 £m	2016 £m
Interest on bank and other deposits	0.2	1.2
Interest receivable from Iberdrola group companies	9.5	9.5
Interest receivable from jointly controlled entities	0.1	0.1
Foreign exchange gains	2.9	10.3
Fair value and other gains on financing derivatives	2.7	3.1
	<b>15.4</b>	<b>24.2</b>

## 29 FINANCE COSTS

	Note	2017 £m	2016 £m
Interest on bank loans and overdrafts		0.1	0.3
Interest on amounts due to Iberdrola group companies		66.5	62.6
Interest on other borrowings		105.4	114.2
Unwinding of discount on provisions		3.4	3.8
Foreign exchange losses		3.2	10.3
Net interest on retirement benefit obligations		9.4	6.8
Fair value and other losses on financing derivatives		3.5	4.7
(Reversal of impairment)/impairment of financial investments		(0.4)	0.6
		<b>191.1</b>	<b>203.3</b>
Capitalised interest	(a)	(16.9)	(19.0)
		<b>174.2</b>	<b>184.3</b>

(a) The tax relief on the capitalised interest for the year ended 31 December 2017 was £1.8 million (2016 £2.1 million).

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 30 INCOME TAX

	2017 £m	2016 £m
Current tax:		
UK Corporation Tax charge on profits for the year	48.2	54.6
Adjustments in respect of prior years	(8.8)	(0.1)
<b>Current tax for the year</b>	<b>39.4</b>	<b>54.5</b>
Deferred tax:		
Origination and reversal of temporary differences	55.1	88.3
Adjustments in respect of prior years	2.1	3.2
Impact of tax rate change	(6.2)	(53.3)
<b>Deferred tax for the year</b>	<b>51.0</b>	<b>38.2</b>
<b>Income tax expense for the year</b>	<b>90.4</b>	<b>92.7</b>

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

	2017 £m	2016 £m
Corporation Tax at 19.25% (2016 20%)	99.4	134.7
Adjustments in respect of prior years	(6.7)	3.1
Impact of tax rate change	(6.2)	(53.3)
Non deductible expenses and other permanent differences	3.9	8.2
<b>Income tax expense for the year</b>	<b>90.4</b>	<b>92.7</b>

The rate of UK Corporation Tax reduced from 20% to 19% on 1 April 2017. Legislation has been enacted to reduce the rate of UK Corporation Tax to 17% on 1 April 2020. This reduces the tax rates expected to apply when temporary differences reverse and impacts the deferred tax charge.

	2017 £m	2016 £m
<b>Comparison of UK Corporation Tax charge and payments</b>		
UK Corporation Tax charge on profits for the year	48.2	54.6
UK Corporation Tax in the consolidated cash flow statement	37.5	107.9

The amount of Corporation Tax paid in the year, shown in the consolidated cash flow statements, and the amount of the Corporation Tax charge for the year are not the same. The main reason for this is the timing of payments. UK Corporation Tax is due in four instalments: two in the year to which the instalment relates, and two in the following year. In addition, the amount in the cash flow statement also includes any refunds received or payments made relating to Corporation Tax liabilities of prior periods.

## 31 DIVIDENDS

	2017 pence per ordinary share	2016 pence per ordinary share	2017 £m	2016 £m
Interim dividend paid	6.8	38.0	300.0	663.0

## 32 CONTINGENT LIABILITIES

### Legal proceedings

The group's businesses are party to various legal claims, actions and complaints, certain of which may involve material amounts. 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 group currently believes that disposition of these matters will not have a materially adverse effect on the consolidated Accounts.

## 33 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 tables below.

	2017						
	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	2023 and thereafter £m	Total £m
Long-term energy purchase contract commitments	3,711.0	616.7	59.9	4.5	–	–	4,392.1
Other contractual commitments	363.4	191.9	72.8	16.5	8.9	63.7	717.2

	2016						
	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 and thereafter £m	Total £m
Long-term energy purchase contract commitments	1,902.2	273.2	19.4	–	–	–	2,194.8
Other contractual commitments	83.3	63.8	26.0	20.6	9.7	3.0	206.4

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 34 RELATED PARTY TRANSACTIONS

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

	2017				2016			
	Ultimate parent (Iberdrola, S.A.) £m	Immediate parent (Scottish Power Limited) £m	Other Iberdrola group companies £m	Jointly controlled entities £m	Ultimate parent (Iberdrola, S.A.) £m	Immediate parent (Scottish Power Limited) (Note (iii)) £m	Other Iberdrola group companies £m	Jointly controlled entities £m
<b>Types of transaction</b>								
Sales and rendering of services	0.5	1.5	72.1	3.6	0.1	1.4	90.8	4.1
Purchases and receipt of services	(37.7)	(1.1)	(127.9)	(11.6)	(38.5)	(2.0)	(179.4)	(12.2)
Finance income	–	9.5	–	0.1	–	9.5	–	0.1
Finance costs	(1.4)	(60.7)	(4.4)	–	(2.3)	(54.6)	(5.7)	–
Net (losses)/gains on foreign exchange	(3.8)	3.8	–	–	(15.1)	15.1	(1.0)	–
Net losses on financing derivatives	–	(0.8)	–	–	–	(1.6)	–	–
Dividends paid	–	(300.0)	–	–	–	(383.0)	(280.0)	–
Changes in the value of cash flow hedges	–	(21.0)	–	–	–	80.1	–	–
<b>Balances outstanding</b>								
Loans receivable	–	565.7	–	–	–	677.7	–	0.3
Trade and other receivables	–	–	8.6	5.3	0.1	–	10.0	1.6
Interest receivable	–	9.6	–	–	–	9.5	–	–
Derivative financial assets	–	8.2	1.8	–	–	48.6	12.0	–
Loans payable	(85.4)	(3,769.9)	–	–	(173.5)	(4,146.0)	(534.6)	–
Trade payables	–	(1.1)	(7.7)	(3.4)	–	–	(37.4)	(6.6)
Capital payables	–	–	(2.1)	–	–	–	(41.5)	–
Interest payable	(0.2)	(59.3)	–	–	(0.9)	(52.6)	(3.6)	–
Derivative financial liabilities	–	(5.3)	(0.4)	–	–	(16.3)	(0.7)	–

(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) Scottish Power UK Holdings Limited was the immediate parent company during the period from 1 January 2016 to 6 July 2016. On 7 July 2016, Scottish Power Limited became the immediate parent company. On 31 March 2016 a dividend of £280.0 million was paid to Scottish Power UK Holdings Limited.

### (b) Remuneration of key management personnel

The remuneration of the key management personnel of the group is set out below. The remuneration of all twelve (2016 twelve) key management personnel, is included within staff costs at Note 25 (a).

	2017 £m	2016 £m
Short-term employee benefits	3.6	3.4
Post-employment benefits	0.4	0.5
Share-based payments	2.3	1.5
	6.3	5.4

### (c) Directors' remuneration

The remuneration of the directors that provided qualifying services to the group is set out below. During the year, all (2016 all) of the directors were remunerated by the group.

	2017 £000	2016 £000
<b>Aggregate remuneration in respect of qualifying services</b>	<b>828</b>	<b>890</b>
Number of directors who exercised share options	3	3
Number of directors who received shares under a long-term incentive scheme	2	2
Number of directors accruing retirement benefits under a defined benefit pension scheme	3	3
<b>Highest paid director</b>	<b>2017 £000</b>	<b>2016 £000</b>
Aggregate remuneration in respect of qualifying services	336	344
Accrued pension benefit	53	49

(i) The highest paid director received shares under a long-term share incentive scheme in both years.

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

### (d) Ultimate parent company

The directors regard Iberdrola, S.A. (incorporated in Spain) 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 the registered office of the company at 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 Limited. Copies of the consolidated Accounts of Scottish Power Limited may be obtained from its registered address, 320 St. Vincent Street, Glasgow, G2 5AD.

In addition to the company's parent undertakings disclosed above, the group's other related undertakings are disclosed in Note 7.

# NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

## 35 AUDITOR REMUNERATION

	2017 £m	2016 £m
Audit of the company and consolidated annual Accounts	0.1	0.1
Audit of the company's subsidiaries pursuant to legislation	0.8	1.2
Audit fees	0.9	1.3
Audit-related assurance services	0.1	0.2
<b>Total</b>	<b>1.0</b>	<b>1.5</b>

- (a) For the year ended 31 December 2017, all fees paid to the group's auditors of £1.0 million (2016 £1.5 million) were charged to the income statement.
- (b) KPMG LLP were appointed auditor of the group and company during 2017, replacing Ernst & Young LLP. Auditor remuneration for 2017 is primarily payable to KPMG LLP and primarily payable to Ernst & Young LLP for 2016.

## 36 GROUP RESTRUCTURING

As part of an Iberdrola group restructuring exercise the following transactions have taken place.

- On 1 August 2017 Iberdrola Renovables France SAS was sold to Iberdrola Eólica Marina, S.A.U. (an indirectly wholly-owned subsidiary of Iberdrola, S.A.) for €24.4 million (equivalent to £21.8 million). Iberdrola Renovables France SAS has a 70% equity holding in one subsidiary, Ailes Marines SAS. As these companies' operations and net assets are not material to the group, they have not been disclosed separately as discontinued operations, as defined in IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' ("IFRS 5"). The impact of the disposal of these companies on the results and net assets of the group is set out below.
- On 1 August 2017 Iberdrola Renovables Deutschland GmbH was sold to Iberdrola Eólica Marina, S.A.U. for €1 (equivalent to £1). Iberdrola Renovables Deutschland GmbH wholly owns two subsidiaries: Iberdrola Renovables Offshore Deutschland GmbH and Baltic Eagle GmbH, which was acquired during 2017. As these companies' operations and net assets are not material to the group they have not been disclosed separately as discontinued operations, as defined in IFRS 5. The impact of the disposal of these companies on the results and net assets of the group is set out below.

Based on the book values of the net assets disposed of, the related proceeds and the effect of recycling of foreign exchange, the gain on disposal attributable to equity holder of the parent is £20.2 million, as summarised below.

	Notes to the Accounts	Total £m
<b>Book values of assets and liabilities at 1 August 2017</b>		
Intangible assets	8	0.4
Property, plant and equipment	9	1,143.5
Deferred tax	24	6.0
Trade and other receivables		8.1
Cash		1.5
Trade and other payables		(271.6)
Current payables due to Iberdrola group companies – loans		(311.1)
Non-current payables due to Iberdrola group companies – loans		(562.4)
Loans and other borrowings		(12.4)
<b>Book value of assets disposed</b>		<b>2.0</b>
<b>Sales proceeds:</b>		
Cash consideration		21.8
<b>Gain on disposal before recycling of foreign exchange (including non-controlling interest)</b>		<b>19.8</b>
Less non-controlling interest	16	(0.1)
Recycling of foreign exchange	15	0.5
<b>Gain on disposal attributable to equity holder of the parent</b>		<b>20.2</b>
The analysis of cash flow in respect of the above disposal is detailed below:		
		£m
Cash consideration		21.8
Cash disposed		(1.5)
<b>Cash inflows on group restructuring (included in cash flows from investing activities)</b>		<b>20.3</b>



## NOTES TO THE CONSOLIDATED ACCOUNTS *continued*

31 December 2017

### 37 GOING CONCERN

The group's business activities together with the factors likely to affect its future development and position are set out in the Strategic Report on pages 1 to 13.

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 £2,573.1 million and net assets of £5,281.4 million at its most recent balance sheet date.

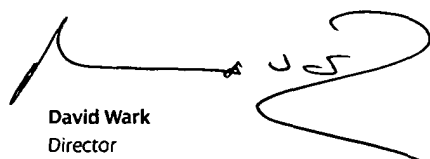
The group is ultimately owned by Iberdrola, S.A. and it participates in the Iberdrola group's centralised treasury arrangements and shares banking facilities with its parent companies and fellow subsidiaries. As a consequence, the group depends, in part, on the ability of the Iberdrola group to continue 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 does not have the ability to, and 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 adopt the going concern basis of accounting in preparing the Accounts.

SCOTTISH POWER UK PLC  
COMPANY BALANCE SHEETS  
at 31 December 2017 and 31 December 2016

	Notes	2017 £m	2016 £m
<b>ASSETS</b>			
<b>NON-CURRENT ASSETS</b>			
Intangible assets	38	19.0	19.7
Property, plant and equipment		51.3	47.5
Property, plant and equipment in use	39	50.6	45.7
Property, plant and equipment in the course of construction	39	0.7	1.8
Trade and other receivables	40	2,497.4	1,739.6
Financial assets		3,395.3	3,255.3
Investments in subsidiaries	41	3,351.6	3,200.7
Other investments	41	0.6	0.7
Derivative financial instruments	43, 50	43.1	53.9
Deferred tax asset	42	104.1	85.4
<b>NON-CURRENT ASSETS</b>		<b>6,067.1</b>	<b>5,147.5</b>
<b>CURRENT ASSETS</b>			
Trade and other receivables	40	318.5	703.9
Current tax receivables		23.3	18.0
Financial assets		1.1	1.3
Derivative financial instruments	43, 50	1.1	1.3
<b>CURRENT ASSETS</b>		<b>342.9</b>	<b>723.2</b>
<b>TOTAL ASSETS</b>		<b>6,410.0</b>	<b>5,870.7</b>
<b>EQUITY AND LIABILITIES</b>			
<b>EQUITY</b>			
Of shareholders of the parent		3,511.8	2,332.1
Share capital	45, 46	2,192.0	872.0
Share premium	46	398.2	398.2
Hedge reserve	46	0.1	0.1
Other reserves	46	8.2	8.2
Retained earnings – opening balance	46	1,053.6	1,286.0
Retained earnings – profit for the year	46	346.2	639.9
Retained earnings – other movements	46	(486.5)	(872.3)
Retained earnings – closing balance	46	913.3	1,053.6
<b>TOTAL EQUITY</b>		<b>3,511.8</b>	<b>2,332.1</b>
<b>NON-CURRENT LIABILITIES</b>			
Provisions		569.2	448.2
Provision for retirement benefit obligations	47	564.8	442.5
Other provisions	48	4.4	5.7
Bank borrowings and other financial liabilities		1,074.9	1,076.5
Loans and other borrowings	49	1,074.9	1,076.5
Trade and other payables	51	69.5	69.3
<b>NON-CURRENT LIABILITIES</b>		<b>1,713.6</b>	<b>1,594.0</b>
<b>CURRENT LIABILITIES</b>			
Provisions	48	3.3	2.7
Bank borrowings and other financial liabilities		1,088.2	1,824.3
Loans and other borrowings	49	1,088.2	1,824.3
Trade and other payables	51	93.1	117.6
<b>CURRENT LIABILITIES</b>		<b>1,184.6</b>	<b>1,944.6</b>
<b>TOTAL LIABILITIES</b>		<b>2,898.2</b>	<b>3,538.6</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>6,410.0</b>	<b>5,870.7</b>

Approved by the board on 27 April 2018 and signed on its behalf by:

  
David Wark  
Director

Notes 1 to 5 and the accompanying Notes 38 to 57 are an integral part of the company balance sheets as at 31 December 2017 and 31 December 2016.

SCOTTISH POWER UK PLC  
 COMPANY STATEMENTS OF COMPREHENSIVE INCOME  
 for the years ended 31 December 2017 and 31 December 2016

	Note	2017 £m	2016 £m
<b>NET PROFIT FOR THE YEAR</b>		<b>346.2</b>	<b>639.9</b>
<b>OTHER COMPREHENSIVE INCOME</b>			
<b>Items that will not be reclassified to the income statement:</b>			
Actuarial losses on retirement benefits:			
Actuarial losses on retirement benefits	46	(222.9)	(251.4)
Tax relating to actuarial losses on retirement benefits	46	36.4	42.1
Cash flow hedges:			
Change in the value of cash flow hedges	46	(0.1)	0.2
Tax relating to cash flow hedges	46	0.1	(0.1)
<b>OTHER COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>(186.5)</b>	<b>(209.2)</b>
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>159.7</b>	<b>430.7</b>

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

COMPANY STATEMENTS OF CHANGES IN EQUITY  
 for the years ended 31 December 2017 and 31 December 2016

	Share capital £m	Share premium £m	Hedge reserve £m	Other reserves £m	Retained earnings £m	Total equity £m
At 1 January 2016	872.0	398.2	–	8.2	1,286.0	2,564.4
Total comprehensive income for the year	–	–	0.1	–	430.6	430.7
Dividends	–	–	–	–	(663.0)	(663.0)
At 1 January 2017	872.0	398.2	0.1	8.2	1,053.6	2,332.1
Total comprehensive income for the year	–	–	–	–	159.7	159.7
Share capital issued	1,320.0	–	–	–	–	1,320.0
Dividends	–	–	–	–	(300.0)	(300.0)
<b>At 31 December 2017</b>	<b>2,192.0</b>	<b>398.2</b>	<b>0.1</b>	<b>8.2</b>	<b>913.3</b>	<b>3,511.8</b>

Notes 1 to 5 and the accompanying Notes 38 to 57 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 2017 and 31 December 2016.

SCOTTISH POWER UK PLC  
COMPANY CASH FLOW STATEMENTS  
for the years ended 31 December 2017 and 31 December 2016

	2017 £m	2016 Restated * £m
Cash flows from operating activities		
Profit before tax	337.3	632.7
Adjustments for:		
Depreciation and amortisation	19.2	20.3
Change in provisions	1.6	(0.1)
Finance income and costs	29.6	30.4
Shareholding income	(378.5)	(663.0)
Net gain on disposal of non-current assets	–	(0.1)
Movement in retirement benefits	(110.0)	(80.1)
Changes in working capital:		
Change in trade and other receivables	8.5	(4.6)
Change in trade and other payables	(11.6)	38.1
Provisions paid	(2.5)	(1.6)
Income taxes received	21.4	15.8
Interest received	69.3	72.7
Dividends received	378.5	663.0
<b>Net cash flows from operating activities (i)</b>	<b>362.8</b>	<b>723.5</b>
Cash flows from investing activities		
Investments in intangible assets	(9.5)	(7.3)
Investments in property, plant and equipment	(12.3)	(34.5)
Proceeds from disposal of property, plant and equipment	0.1	0.3
Net investment in non-current investments	(150.8)	(185.0)
Decrease/(increase) in amounts due from Iberdrola group companies – current loans receivable	375.6	(287.9)
(Increase)/decrease in amounts due from Iberdrola group companies – non-current loans receivable	(758.0)	216.0
<b>Net cash flows from investing activities (ii)</b>	<b>(554.9)</b>	<b>(298.4)</b>
Cash flows from financing activities		
(Decrease)/increase in amounts due from Iberdrola group companies – current loans payable	(531.2)	300.2
Dividends paid to company's equity holder	(300.0)	(663.0)
Cash inflows from borrowings	–	21.1
Share capital issued	1,320.0	–
Interest paid	(90.4)	(83.4)
Repayments of borrowings	(206.3)	–
<b>Net cash flows from financing activities (iii)</b>	<b>192.1</b>	<b>(425.1)</b>
<b>Net cash and cash equivalents (i)+(ii)+(iii)</b>	<b>–</b>	<b>–</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>–</b>	<b>–</b>
<b>Cash and cash equivalents at end of year</b>	<b>–</b>	<b>–</b>

\* Comparative figures have been restated (refer to Note 2).

# NOTES TO THE COMPANY ACCOUNTS

31 December 2017

## 38 INTANGIBLE ASSETS

Year ended 31 December 2016	Computer software (Note (a)) £m	Licences £m	Total £m
<b>Cost:</b>			
At 1 January 2016	97.5	1.1	98.6
Additions	7.3	–	7.3
Disposals	(20.6)	–	(20.6)
<b>At 31 December 2016</b>	<b>84.2</b>	<b>1.1</b>	<b>85.3</b>
<b>Amortisation:</b>			
At 1 January 2016	73.7	0.2	73.9
Amortisation for the year	11.8	0.4	12.2
Disposals	(20.5)	–	(20.5)
<b>At 31 December 2016</b>	<b>65.0</b>	<b>0.6</b>	<b>65.6</b>
<b>Net book value:</b>			
At 31 December 2016	19.2	0.5	19.7
At 1 January 2016	23.8	0.9	24.7

Year ended 31 December 2017	Computer software (Note (a)) £m	Licences £m	Total £m
<b>Cost:</b>			
At 1 January 2017	84.2	1.1	85.3
Additions	9.5	–	9.5
Disposals	(0.6)	–	(0.6)
<b>At 31 December 2017</b>	<b>93.1</b>	<b>1.1</b>	<b>94.2</b>
<b>Amortisation:</b>			
At 1 January 2017	65.0	0.6	65.6
Amortisation for the year	9.8	0.4	10.2
Disposals	(0.6)	–	(0.6)
<b>At 31 December 2017</b>	<b>74.2</b>	<b>1.0</b>	<b>75.2</b>
<b>Net book value:</b>			
At 31 December 2017	18.9	0.1	19.0
At 1 January 2017	19.2	0.5	19.7

(a) The cost of fully amortised computer software still in use at 31 December 2017 was £52.3 million (2016 £36.3 million).

# NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

## 39 PROPERTY, PLANT AND EQUIPMENT

### (a) Movements in property, plant and equipment

Year ended 31 December 2016	Property, plant and equipment in use (Note (i)) £m	Plant in progress (Note (ii)) £m	Total £m
<b>Cost:</b>			
At 1 January 2016	72.6	3.4	76.0
Additions	12.3	17.2	29.5
Transfers from progress to plant in use	18.8	(18.8)	–
Disposals	(14.4)	–	(14.4)
<b>At 31 December 2016</b>	<b>89.3</b>	<b>1.8</b>	<b>91.1</b>
<b>Depreciation:</b>			
At 1 January 2016	49.7	–	49.7
Charge for the year	8.1	–	8.1
Disposals	(14.2)	–	(14.2)
<b>At 31 December 2016</b>	<b>43.6</b>	<b>–</b>	<b>43.6</b>
<b>Net book value:</b>			
At 31 December 2016	45.7	1.8	47.5
At 1 January 2016	22.9	3.4	26.3
The net book value of property, plant and equipment at 31 December 2016 is analysed as follows:			
Property, plant and equipment in use	45.7	–	45.7
Property, plant and equipment in the course of construction	–	1.8	1.8
	45.7	1.8	47.5

Year ended 31 December 2017	Property, plant and equipment in use (Note (i)) £m	Plant in progress (Note (ii)) £m	Total £m
<b>Cost:</b>			
At 1 January 2017	89.3	1.8	91.1
Additions	10.7	2.2	12.9
Transfers from progress to plant in use	3.3	(3.3)	–
Disposals	(9.2)	–	(9.2)
<b>At 31 December 2017</b>	<b>94.1</b>	<b>0.7</b>	<b>94.8</b>
<b>Depreciation:</b>			
At 1 January 2017	43.6	–	43.6
Charge for the year	9.0	–	9.0
Disposals	(9.1)	–	(9.1)
<b>At 31 December 2017</b>	<b>43.5</b>	<b>–</b>	<b>43.5</b>
<b>Net book value:</b>			
At 31 December 2017	50.6	0.7	51.3
At 1 January 2017	45.7	1.8	47.5
The net book value of property, plant and equipment at 31 December 2017 is analysed as follows:			
Property, plant and equipment in use	50.6	–	50.6
Property, plant and equipment in the course of construction	–	0.7	0.7
	50.6	0.7	51.3

(i) The 'Property, plant and equipment in use' category principally comprises fixtures and fittings and IT equipment.

(ii) In the current year, the 'Plant in progress' category comprises costs in relation to smart meter infrastructure. In 2016 this category primarily comprised costs in relation to fixtures and fittings.

(iii) The cost of fully depreciated property, plant and equipment still in use at 31 December 2017 was £24.4 million (2016 £26.1 million).

# NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

## 39 PROPERTY, PLANT AND EQUIPMENT *continued*

### (b) Operating lease arrangements

(i) Operating lease commitments	2017 £m	2016 £m
The future minimum discounted lease payments under non-cancellable operating leases are as follows:		
Within one year	13.5	13.5
Between one and five years	35.4	40.8
More than five years	88.0	92.4
	136.9	146.7

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

(ii) Operating lease receivables	2017 £m	2016 £m
The future minimum discounted lease payments receivable under non-cancellable operating leases are as follows:		
Within one year	0.8	0.7
Between one and five years	0.9	0.5
	1.7	1.2

The company leases buildings 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.

(c) Capital commitments	2017 £m	2016 £m
Contracted but not provided	0.3	3.2

## 40 TRADE AND OTHER RECEIVABLES

	Notes	2017 £m	2016 £m
<b>Current receivables:</b>			
Receivables due from Iberdrola group companies – trade		10.7	17.2
Receivables due from Iberdrola group companies – loans	(a)	259.2	634.8
Receivables due from Iberdrola group companies – interest		28.4	29.9
Trade receivables		10.7	12.7
Prepayments		9.5	9.3
		318.5	703.9
<b>Non-current receivables:</b>			
Receivables due from Iberdrola group companies – loans	(a)	2,452.0	1,694.0
Prepayments		6.3	7.8
Other receivables	(b)	39.1	37.8
		2,497.4	1,739.6

(a) Current loans due from Iberdrola group companies includes £67.2 million (2016 £418.8 million) repayable on demand with interest payable at 1% above the Bank of England base rate. The non-current loans with Iberdrola group companies due to mature in 2022, 2023 and 2025 are repayable in equal instalments on a bi-annual basis. The instalment of £192.0 million due in 2018 on the loans with a final maturity of 2022 is classified as current at 31 December 2017 and the instalment of £216.0 million paid in 2017 on the loans with final maturity dates of 2023 and 2025 was classified as current at 31 December 2016.

(b) This balance represents other receivables recognised as part of a contractual renegotiation.

(c) The company utilises forms of collateral to manage its credit exposure. At 31 December 2017, the company held letters of credit of £nil (2016 £13.5 million).

(d) At 31 December 2017 trade receivables of £6.5 million (2016 £11.8 million) were past due but not impaired:

	2017 £m	2016 £m
<b>Past due but not impaired:</b>		
Less than 3 months	6.4	11.7
Between 3 and 6 months	–	0.1
After more than 12 months	0.1	–
	6.5	11.8

## NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

### 41 INVESTMENTS

	Notes	Investments in subsidiaries £m	Other investments (Note (a)) £m	Total £m
At 1 January 2016		3,015.7	0.7	3,016.4
Additions	(b)	185.0	–	185.0
At 1 January 2017		3,200.7	0.7	3,201.4
Additions	(c)	160.0	–	160.0
Disposals	(d)	(9.1)	(0.1)	(9.2)
<b>At 31 December 2017</b>		<b>3,351.6</b>	<b>0.6</b>	<b>3,352.2</b>

- (a) At 31 December 2017 the company held £0.6 million (2016 £0.7 million) of investments for which no quoted market price is available and whose fair value could not be reliably measured.
- (b) On 24 October 2016 the company subscribed for and was allotted an additional 185,000,000 ordinary shares of £1 each in ScottishPower Energy Networks Holdings Limited for a consideration of £185.0 million.
- (c) On 11 December 2017, the company subscribed for and was allotted an additional 160,000,000 ordinary shares of £1 each in Scottish Power Renewables (UK) Limited for a consideration of £160.0 million.
- (d) During 2017, certain of the company's dormant subsidiaries were dissolved resulting in the write-off of £9.1 million of investments.
- (e) The company's subsidiary and joint venture holdings are listed in Note 7.

### 42 DEFERRED TAX ASSET

Deferred tax recognised in the Accounts is as follows:

	Property, plant and equipment £m	Derivative financial instruments £m	Retirement benefits £m	Other temporary differences £m	Total £m
At 1 January 2016	4.5	–	52.9	0.6	58.0
Charge to income statement	(1.3)	–	(12.9)	(0.4)	(14.6)
Recorded in the statement of comprehensive income	–	(0.1)	42.1	–	42.0
At 1 January 2017	3.2	(0.1)	82.1	0.2	85.4
Charge to income statement	(0.2)	–	(19.2)	1.6	(17.8)
Recorded in the statement of comprehensive income	–	0.1	36.4	–	36.5
<b>At 31 December 2017</b>	<b>3.0</b>	<b>–</b>	<b>99.3</b>	<b>1.8</b>	<b>104.1</b>

- (a) At 31 December 2017, the company had unutilised capital losses of £5.3 million (2016 £5.4 million). No deferred tax has been recognised in the Accounts due to the unpredictability of suitable future profit streams against which these losses may be utilised.
- (b) Legislation has been enacted to reduce the rate of the UK Corporation Tax to 17% on 1 April 2020. This reduces the tax rates expected to apply when temporary differences reverse and impacts the deferred tax charge.

### 43 FINANCIAL INSTRUMENTS

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

	Notes	2017		2016	
		Carrying Amount £m	Fair Value £m	Carrying Amount £m	Fair Value £m
<b>Financial assets</b>					
Derivative financial instruments	(a)	44.2	44.2	55.2	55.2
Current receivables	(b)	309.0	309.0	694.6	694.6
Non-current receivables	(b), (c)	2,491.1	2,781.7	1,731.8	2,113.0
Other investments		0.6	0.6	0.7	0.7
<b>Financial liabilities</b>					
Loans and other borrowings	(d)	(2,163.1)	(2,415.6)	(2,900.8)	(3,182.2)
Payables	(b)	(123.5)	(123.5)	(142.5)	(142.5)

The carrying amount of these financial instruments is calculated as set out in Note 3C. With the exception of non-current receivables and loans and other borrowings, the carrying value of financial instruments is a reasonable approximation of fair value. The fair value of non-current receivables is calculated as set out in footnote (c). The fair value of loans and other borrowings is calculated as set out in footnote (d), which is categorised as level 2 in the fair value hierarchy.

- (a) Further detail on derivative financial instruments is disclosed in Note 50.
- (b) Balances outwith the scope of IFRS 7 have been excluded, principally prepayments, payments received on account and other tax payables.
- (c) The fair value of non-current receivables relating to loans due from Iberdrola group companies is calculated using a discounted cash flow.
- (d) 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 were Level 2 in both the current and prior year. Level 2 foreign exchange derivatives comprises cross currency swaps and forward foreign exchange contracts which are fair valued using exchange rates that are quoted in an active market.



## NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

### 44 LIQUIDITY ANALYSIS

#### Maturity profile of financial liabilities

The table below summarises the maturity profile of the company's financial liabilities based on contractual undiscounted cash flows.

Cash outflows	Note	2017					Total £m
		2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	2023 and thereafter £m
Loans and other borrowings		1,166.0	57.1	57.4	349.0	40.5	1,053.5
Payables	(a)	38.7	9.2	5.5	25.4	0.2	79.0
		1,204.7	66.3	62.9	374.4	40.7	1,053.5
							2,802.5

Cash outflows	Note	2016					Total £m
		2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 and thereafter £m
Derivative financial instruments		0.6	–	–	–	–	0.6
Loans and other borrowings		1,919.1	56.8	57.1	57.3	348.8	1,072.1
Payables	(a)	46.1	11.1	8.9	5.2	13.5	–
		1,965.8	67.9	66.0	62.5	362.3	1,072.1
							3,596.6

(a) Contractual cash flows exclude accrued interest as these cash flows are included within loans and other borrowings.

### 45 SHARE CAPITAL

	2017 £m	2016 £m
<b>Allotted, called up and fully paid:</b>		
4,383,983,102 ordinary shares of 50p each (2016 1,743,983,102)	2,192.0	872.0

(a) On 5 October 2017, the company issued 2,640,000,000 ordinary shares of 50p each to its immediate parent, Scottish Power Limited, for a total consideration of £1,320.0 million.

### 46 ANALYSIS OF MOVEMENTS IN EQUITY ATTRIBUTABLE TO THE EQUITY HOLDER OF SCOTTISH POWER UK PLC

	Share Capital (Note (a)) £m	Share premium (Note (b)) £m	Hedge reserve (Note (c)) £m	Other reserves (Note (d)) £m	Retained earnings (Note (e)) £m	Total £m
At 1 January 2016	872.0	398.2	–	8.2	1,286.0	2,564.4
Profit for the year attributable to the equity holder of Scottish Power UK plc	–	–	–	–	639.9	639.9
Changes in the value of cash flow hedges	–	–	0.2	–	–	0.2
Tax relating to cash flow hedges	–	–	(0.1)	–	–	(0.1)
Actuarial losses on retirement benefits	–	–	–	–	(251.4)	(251.4)
Tax relating to actuarial losses on retirement benefits	–	–	–	–	42.1	42.1
Dividends	–	–	–	–	(663.0)	(663.0)
At 1 January 2017	872.0	398.2	0.1	8.2	1,053.6	2,332.1
Profit for the year attributable to the equity holder of Scottish Power UK plc	–	–	–	–	346.2	346.2
Share capital issued	1,320.0	–	–	–	–	1,320.0
Changes in the value of cash flow hedges	–	–	(0.1)	–	–	(0.1)
Tax relating to cash flow hedges	–	–	0.1	–	–	0.1
Actuarial losses on retirement benefits	–	–	–	–	(222.9)	(222.9)
Tax relating to actuarial losses on retirement benefits	–	–	–	–	36.4	36.4
Dividends	–	–	–	–	(300.0)	(300.0)
At 31 December 2017	2,192.0	398.2	0.1	8.2	913.3	3,511.8

(a) On 5 October 2017, the company issued 2,640,000,000 ordinary shares of 50p each to its immediate parent, Scottish Power Limited, for a total consideration of £1,320.0 million.

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

(c) 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 value of a non-financial asset.

(d) Other reserves as at 31 December 2017 comprises a capital redemption reserve of £8.2 million (2016 £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.

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

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

	Foreign exchange rate hedges £m	Tax effect £m	Total £m
At 1 January 2016	–	–	–
Effective cash flow hedges recognised	0.3	(0.1)	0.2
Removed from equity and recognised in the carrying amount of hedged items	(0.1)	–	(0.1)
At 1 January 2017	0.2	(0.1)	0.1
Effective cash flow hedges recognised	(0.1)	0.1	–
At 31 December 2017	0.1	–	0.1

(g) All amounts included in the hedge reserve at 31 December 2017 are due to mature within one year (2016 due within one year).

# NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

## 47 RETIREMENT BENEFIT OBLIGATIONS

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

	2017 £m	2016 £m
Non-current liabilities	564.8	442.5

(a) 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 18 of the group financial statements.

## 48 OTHER PROVISIONS

Year ended 31 December 2016	Notes	At 1 January 2016 £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	Released during year £m	At 31 December 2016 £m
Onerous contracts	(a)	8.6	0.2	0.2	(1.4)	(0.3)	7.3
Other	(b)	1.3	–	–	(0.2)	–	1.1
		9.9	0.2	0.2	(1.6)	(0.3)	8.4

Year ended 31 December 2017	Notes	At 1 January 2017 £m	New provisions £m	Unwinding of discount £m	Utilised during year £m	At 31 December 2017 £m
Onerous contracts	(a)	7.3	0.2	0.2	(2.3)	5.4
Reorganisation and restructuring	(c)	–	1.4	–	–	1.4
Other	(b)	1.1	–	–	(0.2)	0.9
		8.4	1.6	0.2	(2.5)	7.7

Analysis of total other provisions	2017 £m	2016 £m
Non-current	4.4	5.7
Current	3.3	2.7
	7.7	8.4

(a) The provision for 'Onerous contracts' relates to various property leases. The leases will expire between 2018 and 2025.

(b) The 'Other' category comprises various provisions which are not individually sufficiently material to warrant separate disclosure.

(c) The new provision for 'Reorganisation and restructuring' relates to a group wide restructuring programme and is expected to be utilised in 2018.

## 49 LOANS AND OTHER BORROWINGS

Analysis by instrument and maturity	Notes	Interest rate*	Maturity	2017 £m	2016 £m
Loans with Iberdrola group companies		Base + 1%	On demand	1,045.0	1,576.2
£200 million euro-sterling bond	(b)	8.375%	20 February 2017	–	200.0
Collateral		LIBOR	17 June 2018	44.0	50.3
£300 million medium-term note	(c)	5.9%	22 February 2021	297.9	297.2
£250 million euro-sterling bond	(b), (d)	6.75%	29 May 2023	249.1	248.9
£175 million inflation linked bond	(c)	3.494% x RPI	13 October 2024	283.3	273.6
10 billion JPY loan	(e)	4.6%	27 July 2029	93.8	104.6
£50 million medium-term note	(c)	5.75%	9 December 2039	50.0	50.0
£100 million medium-term note	(c)	6.375%	31 May 2041	100.0	100.0
				2,163.1	2,900.8

\* Base – Bank of England Base Rate; LIBOR – London Inter-Bank Offer Rate; RPI – Retail Price Index

Analysis of loans and other borrowings	Note	2017 £m	2016 £m
Non-current		1,074.9	1,076.5
Current	(a)	1,088.2	1,824.3
		2,163.1	2,900.8

(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, 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 £(0.8) million (2016 £(2.2) 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) 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.

(d) The euro-sterling bond due 2023 can be redeemed at any time by the company at the higher of the principal amount or redemption price (as determined by HSBC Bank plc) giving 30 to 45 days' notice to the lender.

(e) 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.

(f) The company has no undrawn committed borrowing facilities at 31 December 2017 (2016 nil).

# NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

## 49 LOANS AND OTHER BORROWINGS *continued*

### (g) Reconciliation of movements of liabilities to cash flows arising from financing activities

	Liabilities			Total £m
	Loans and other borrowings (Current) £m	Loans and other borrowings (Non-current) £m	Interest payable (Current) (Note (ii)) £m	
<b>At 1 January 2017</b>	<b>1,824.3</b>	<b>1,076.5</b>	<b>57.7</b>	<b>2,958.5</b>
Decrease in amounts due to Iberdrola group companies	(531.2)	–	–	(531.2)
Repayments of borrowings	(206.3)	–	–	(206.3)
Interest paid	–	–	(90.4)	(90.4)
<b>Total movements from financing cash flows</b>	<b>(737.5)</b>	<b>–</b>	<b>(90.4)</b>	<b>(827.9)</b>
Fair value and other non-cash movements	1.4	(1.6)	(20.3)	(20.5)
Other movements	–	–	97.5	97.5
<b>Total liability-related other movements</b>	<b>1.4</b>	<b>(1.6)</b>	<b>77.2</b>	<b>77.0</b>
<b>At 31 December 2017</b>	<b>1,088.2</b>	<b>1,074.9</b>	<b>44.5</b>	<b>2,207.6</b>

(i) External interest payable of £23.7 million (2016 £38.2 million) and internal interest payable of £20.8 million (2016 £19.5 million) are included within Trade and other payables (refer to Note 51).

## 50 DERIVATIVE FINANCIAL INSTRUMENTS

### Analysis of derivative financial instruments – carrying value

	Note	2017		2016	
		Current	Non-current	Current	Non-current
<b>Hedging derivatives: Exchange rate hedges</b>					
Fair value hedge – Currency swap	(a)	1.1	43.1	1.1	53.9
Fair value hedge – Foreign exchange		–	–	0.2	–
<b>Total derivatives in the balance sheet</b>		<b>1.1</b>	<b>43.1</b>	<b>1.3</b>	<b>53.9</b>

(a) At 31 December 2017 the company held cash collateral of £44.0 million (2016 £50.3 million) in respect of derivatives.

## 51 TRADE AND OTHER PAYABLES

	Note	2017 £m	2016 £m
<b>Current trade and other payables:</b>			
Payables due to Iberdrola group companies – trade		9.6	15.5
Payables due to Iberdrola group companies – interest		20.8	19.5
Trade payables		17.0	19.8
Other taxes and social security		8.6	12.5
Payables received on account		1.3	1.3
Capital payables		6.3	5.7
Other payables		29.5	43.3
		<b>93.1</b>	<b>117.6</b>
<b>Non-current other payables:</b>			
Payables due to Iberdrola group companies – trade	(a)	39.1	37.8
Payables received on account		29.2	30.6
Other payables		1.2	0.9
		<b>69.5</b>	<b>69.3</b>

(a) This balance represents other payables recognised as part of a contractual renegotiation.

## 52 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 27 April 2018. The profit for the financial year per the Accounts of the company was £346.2 million (2016 £639.9 million).

## NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

### 53 EMPLOYEE INFORMATION

#### (a) Staff costs

	2017 £m	2016 £m
Wages and salaries	29.8	28.0
Social security costs	3.4	3.0
Pension and other costs	25.7	12.5
<b>Total staff costs</b>	<b>58.9</b>	<b>43.5</b>
Less: capitalised staff costs	(0.7)	(0.8)
<b>Charged to the income statement</b>	<b>58.2</b>	<b>42.7</b>

#### (b) Employee numbers

Details of the year end and average number of employees (full and part time) employed by the company, including UK based directors, can be found within the Corporate category of Note 25(b).

#### (c) Pensions

The company's contributions in the year were £6.9 million (2016 £5.8 million). The company contributes to the group's defined benefit and defined contribution schemes in the UK. Full details of these schemes can be found in Note 18.

### 54 AUDITOR REMUNERATION

The auditors' remuneration of the ScottishPower 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 2017, £20,000 (2016 £33,000) related to the audit of the company Accounts. The total auditors' remuneration for the group is disclosed in Note 35 to the consolidated Accounts.

### 55 DIVIDENDS

	2017 pence per ordinary share	2016 pence per ordinary share	2017 £m	2016 £m
Interim dividend paid	6.8	38.0	300.0	663.0

### 56 FINANCIAL COMMITMENTS

	2017						Total £m
	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	2023 and thereafter £m	
Other contractual commitments	35.3	28.9	24.0	9.1	3.0	3.0	103.3

	2016						Total £m
	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 and thereafter £m	
Long-term energy purchase contract commitments	0.5	–	–	–	–	–	0.5
Other contractual commitments	35.0	29.8	23.3	19.6	8.7	3.0	119.4

# NOTES TO THE COMPANY ACCOUNTS *continued*

31 December 2017

## 57 RELATED PARTY TRANSACTIONS

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

	2017				2016			
	Ultimate parent company (Iberdrola, S.A.) £m	Immediate parent (Scottish Power Limited) £m	Subsidiary companies £m	Other Iberdrola group companies £m	Ultimate parent company (Iberdrola, S.A.) £m	Immediate parent (Scottish Power Limited (Note (ii)) £m	Subsidiary companies £m	Other Iberdrola group companies £m
<b>Types of transaction</b>								
Sales and rendering of services	0.5	1.5	175.3	4.5	0.1	1.4	166.4	4.4
Purchases and receipt of services	(37.5)	–	(3.7)	–	(37.0)	–	(1.5)	(0.1)
Finance income	–	–	67.8	–	–	–	72.8	–
Finance costs	–	(20.8)	–	–	–	(19.4)	(0.7)	–
Change in the value of cash flow hedge reserve	–	0.2	–	–	–	0.2	–	–
Dividends received	–	–	378.5	–	–	–	663.0	–
Dividends paid	–	(300.0)	–	–	–	(383.0)	–	(280.0)
Pensions contributions received	–	–	142.6	–	–	–	90.3	–
<b>Balances outstanding</b>								
Loans receivable	–	–	2,711.2	–	–	–	2,328.8	–
Trade receivables	–	–	10.2	0.5	–	–	9.7	7.5
Interest receivable	–	–	28.4	–	–	–	29.9	–
Derivative financial assets	–	–	–	–	–	0.2	–	–
Loans payable	–	(1,020.8)	(24.2)	–	–	(1,559.5)	(16.7)	–
Trade payables	–	–	(48.7)	–	–	–	(53.3)	–
Interest payable	–	(20.8)	–	–	–	(19.3)	(0.2)	–

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

(ii) Scottish Power UK Holdings Limited was the immediate parent company during the period from 1 January 2016 to 6 July 2016. On 7 July 2016, Scottish Power Limited became the immediate parent company. On 31 March 2016 a dividend of £280.0 million was paid to Scottish Power UK Holdings Limited.

### (b) Remuneration of key management personnel

The remuneration of the key management personnel of the company is set out below. As all three (2016 three) of the key management personnel are remunerated for their work for the ScottishPower group, it has not been possible to apportion their remuneration specifically in respect of their services to this company. During the year all (2016 all) of the key management personnel were remunerated by the company.

	2017 £m	2016 £m
Short-term employee benefits	0.7	0.8
Post-employment benefits	0.2	0.2
Share-based payments	0.5	0.3
	1.4	1.3

### (c) Directors' remuneration

Details of directors' remuneration are set out at Note 34(c).

### (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 Limited.

Copies of the consolidated Accounts of Iberdrola, S.A. may be obtained from Iberdrola, S.A., at its registered office, Torre Iberdrola, Plaza Euskadi 5, 48009, Bilbao, Spain. Copies of the consolidated Accounts of Scottish Power Limited may be obtained from its registered office, 320 St. Vincent Street, Glasgow, G2 5AD.

In addition to the parent undertakings disclosed above, the company's other related undertakings are disclosed in Note 7.

**Scottish Power UK plc**

Registered office: 320 St. Vincent Street, Glasgow, G2 5AD

Registered in Scotland: No. SC117120