Western Power Distribution (South Wales) plc

Regulatory Financial Statements

for the year ended 31 March 2008

WESTERN POWER DISTRIBUTION
Serving the South West and Wales

Western Power Distribution (South Wales) plc

Regulatory Financial Statements

Table of contents

1 Foreword

The main activity of Western Power Distribution (South Wales) plc ("WPD South Wales" or the "Company") is the distribution of electricity within its service area of South and West Wales. It is one of twelve licensed distribution network operators ("DNOs") within England and Wales.

Each DNO is a natural monopoly regulated by the Gas and Electricity Markets Authority (known as "Ofgem"). It is therefore subject to control on the prices it can charge. The principal legislation governing the structure of the electricity industry in Great Britain is the Electricity Act 1989, as amended by the Utilities Act 2000 and the Energy Act 2004. This legislation provides for a licence framework in which the operations of the DNOs are regulated, pursuant to which income generated is subject to an allowed revenue regulatory framework that provides economic incentives to minimise operating, capital and financing costs consistent with the DNOs providing an acceptably reliable distribution network and meeting their legal responsibilities. This licence framework is overseen by Ofgem.

Licences which govern DNOs require each DNO to produce regulatory accounts. These comprise two documents:

- Regulatory Financial Statements; and

- Regulatory Reporting Pack ("RRP").

The purpose of the *Regulatory Financial Statements* is to provide financial information on the same basis as that under the normal financial policies of the DNO. The financial statements themselves are in a similar format to a company's statutory accounts prepared under the Companies Act. This document contains these audited Regulatory Financial Statements.

The RRP was largely developed during the latest price review, which concluded in November 2004 and is effective 1 April 2005. The RRP should better monitor performance against assumptions used in the last price review, and better inform the next price review. The level of detail should highlight the cost drivers within a DNO and thus ensure that the regulated allowance better reflects this. The RRP for 2007/08 will be sent to Ofgem during July 2008.

2 Operating and Financial Review for the year to 31 March 2008

Introduction

Western Power Distribution Holdings Limited is the parent of a group ("WPD" or "Group") whose principal activity is undertaken by WPD South Wales and Western Power Distribution (South West) plc ("WPD South West").

WPD South Wales distributes electricity to approximately 1.1 million end-users over an area of 11,900 square kilometres in the South and West of Wales. It has a resident population of approximately 2.2 million.

Electricity distribution is the transport at a regional level of electricity at reducing voltages from national grid bulk supply points to final end users. A limited volume of electricity also enters the distribution network from embedded generation within WPD South Wales' area, such as windfarms and small hydro-electric plants.

The 1.1 million end-users are registered with licensed electricity suppliers, who in turn pay WPD South Wales for using its network.

WPD South Wales' network comprises 18,235 kilometres of overhead line, 16,591 kilometres of underground cable, service lines into customer premises, and 39,494 transformers.

During 2007/08, the maximum demand recorded was 2,179 megawatts (2006/07: 2,151 megawatts).

Overview

WPD South Wales is a monopoly regulated by licence and operates under a price control regime. The current electricity distribution price control agreed with Ofgem commenced on 1 April 2005 and covers the five year period until 31 March 2010. As part of the review, Ofgem confirmed its intention to continue with the inflation adjusted RPI - X form of price control. WPD South Wales was allowed to increase its prices by inflation plus 6.2% (i.e. "P0" = +6.2%) from 1 April 2005. In each of the subsequent four years prices are allowed to increase by no more than the rate of inflation (i.e. X = 0).

The allowed increase in revenue was in recognition of a number of additional cost challenges that distribution businesses will face over the five year period, particularly in relation to increased investment requirements together with additional tax and pension costs. In comparative terms, the WPD Group was allowed the second highest aggregate P0 rise in the sector and many of the additional cost pressures identified are "pass through" costs which fall on WPD and which Ofgem has allowed WPD to recover. If these are excluded, then WPD has effectively suffered an underlying P0 price reduction of approximately 3%.

The current price control maintains the emphasis on achieving further efficiencies in day to day running costs although at a lower scale than previous reviews with a 1.5% per annum overall reduction in underlying costs required. The current price control also places a greater emphasis on performance than previous reviews and incorporates incentive mechanisms to encourage the reduction of electrical losses and improve the quality of service for customers particularly in relation to the number and duration of interruptions and the quality of telephone response.

Overview (continued)

Ofgem has commenced preparation for the next price control review period commencing 1 April 2010 and in March 2008 they published an initial consultation document covering the key policy areas they wish to look at as part of the fifth electricity distribution price control review. The policy areas are broadly defined as being either customer, environment, network or finance related. As part of the review process Ofgem has established a number of joint industry working groups and workshops to tackle specific policy issues such as regulatory cost reporting, future network security, reviewing electricity distribution commercial arrangements and competition in connections. WPD is pleased to play an active role in supporting these work streams and is providing a leading role in addressing a number of the key network issues for the future. The timetable for the 2010 price control review indicates that Ofgem will publish final proposals in November/December 2009.

The focus for the business during the year has been to continue to concentrate on the four key goals of safety, customer service, network reliability and business efficiency. Continued pressure on overheads, particularly at corporate level, with minimal impact on field staff, has ensured that customer service is not affected and customer service measures remain at an all time high. Operationally, the WPD Group has completed another successful year and continues to be a frontier performer in terms of network reliability despite a year of challenging weather conditions. Ofgem acknowledged WPD's exceptional operating performance during the price control review process and in recognition of WPD's strong performance within the sector rewarded WPD with a 1% P0 increase as part of the price control mechanism and this was included in the P0 change outlined above.

A combination of targeted investment and close monitoring of performance has ensured that we have out-performed in all areas of the business. During the year we exceeded all of Ofgem's National Customer Guarantee Service Standards and met all of our targets under the Quality of Service incentive scheme by a significant margin. A series of road show presentations by the directors each year ensure that all staff within the WPD Group are aware of, and can contribute to, the corporate goals of safety, network reliability, customer service and business efficiency.

Safety

WPD continues to place a strong emphasis on the safety culture within the business and a clear commitment to safety from the "top down" remains an imperative. The focus within the business is to keep the safety message at the top of our agenda. WPD continues to play an active role in many national committees and steering groups which concentrate on the future of safety and training policies across the industry.

The number of lost time accidents to staff working in WPD South Wales was zero in 2007/8 compared with 4 in 2006/7. WPD South West and WPD South Wales together achieved 16 months, from 12 October 2006 to 18 February 2008, which were entirely free of lost time accidents. It is believed that this is a unique achievement among comparable DNOs in the UK. Non lost time accidents for the WPD Group fell from 52 to 43, a reduction of 17%. These are the lowest numbers of accidents recorded within WPD ever.

Safety (continued)

A number of key initiatives have been instigated across the WPD Group in recent years which have helped maintain safety at the forefront of all of our activities. These include implementation of a new WPD Safety Policy Statement, a three year safety plan, and also formulation of new policies covering risk assessment and safety management. Looking ahead remains a key aspect of safety policy at WPD. Developed with the Company HESAC (health and safety committee), the current safety plan identifies a number of priorities for 2008 including a review of safety arrangements for contractors, a revised set of risk assessment and "near miss" reporting requirements, and a reissue of the WPD Distribution Safety Rules.

The safety of the public has also been a major area of activity with over 10,000 copies of a video and leaflet about the dangers of overhead power lines being sent out to companies operating in our service area. A further 7,000 copies of a new WPD video about the risks associated with live underground cables have also been posted. Both videos were produced in-house by WPD staff and continue to be provided free of charge to anyone who is likely to benefit from the information.

WPD runs an annual safety competition for staff where teams are encouraged to develop safety initiatives and to suggest ideas. In addition, a cash prize for charity is offered to the teams that achieve the highest number of accident free days. The Company takes its role of educating the public about the dangers of electricity very seriously and this is an integral part of WPD's wider community support policy. Young people are very much the target and WPD regularly attends Crucial Crew and Junior Life Skills events where representatives join together with members of the emergency services to educate children about the risks associated with electricity. In addition, staff from the Company visit schools in areas where vandalism or incidents have occurred to reinforce the safety message.

WPD also conforms to OHSAS 18001 Occupational Health and Safety Management Systems, which is similar to the more widely recognised ISO 9001 quality standard. This is an indication that WPD health and safety management systems meet the standards expected by law and by the Health and Safety Executive.

Network performance

Performance of the distribution network is measured in two key ways:

Security - the number of supply interruptions recorded per 100 connected customers ("CI"); and

Availability - the number of customer minutes lost per connected customer ("CML").

All licensees who operate a distribution system are required to report annually to Ofgem on their performance in maintaining system Security and Availability. The Quality of Service incentive scheme, also known as the Information and Incentives Scheme ("IIS") which was introduced by Ofgem in April 2002, financially incentivises all licensees including WPD with respect to both the Security and Availability of supply delivered to customers. In addition Ofgem incentivises the quality of telephone response customers receive when they contact the licensee. This is assessed by a customer survey carried out on a monthly basis.

2 Operating and Financial Review for the year to 31 March 2008

Network performance (continued)

Network performance reported to Ofgem for the year is as follows:

	Total	Target
Minutes lost per customer 2007/08	41.9	
Excluded events	-	
IIS Performance 2007/08	**41.9**	**72.2**
IIS Performance 2006/07	47.7	72.2
Interruptions per 100 customers 2007/08	77.7	
Excluded events	-	
IIS Performance 2007/08	**77.7**	**96.8**
IIS Performance 2006/07	83.5	98.2

The figures above cover all reportable interruptions longer than three minutes in duration occurring on the WPD South Wales network including those caused by bad weather and other faults together with 50% of CI and CML due to pre-arranged shutdowns for maintenance and construction. The 11kV network is the principal driver of customer minutes lost, with faults on overhead lines being the major contributor. In addition to the performance reported under IIS above, 87.5% of customers off supply in South Wales as the result of a high voltage ("HV") fault were restored within one hour of the fault occurring. We believe that the WPD Group has the best one hour restoration performance of any DNO.

Under the IIS scheme, performance is targeted at an underlying level of improvement. DNOs are thus permitted to claim an adjustment for events during the year which they believe were exceptional and had a significant impact on the total reported performance. An exceptional event can either be caused by a large number of weather related faults or be due to a one-off event which is outside of the DNO's control. In either case, the event must meet prescribed thresholds in terms of the numbers of faults experienced or, for a one-off event, in terms of either the number of customers affected or the duration of the incident. If an event meets these prescribed thresholds, the DNO must notify Ofgem who will conduct an audit to determine the impact of the event. As part of the audit process the DNO must demonstrate that it mitigated against the impact of the event to the best of its ability before Ofgem will exclude the CI and CML incurred. WPD South Wales reported no exceptional events to Ofgem during the year.

Subject to Ofgem confirmation, our IIS CML and CI of 41.9 customer minutes lost and 77.7 interruptions per 100 customers for the year are within our targets of 72.2 and 96.8 respectively. The low level of CML relative to the target set by Ofgem is particularly gratifying as it shows the results of our focus on operational excellence and has been achieved in a year when the number of weather related network faults increased significantly and we faced a number of operational challenges related to restoring customers in difficult working conditions.

Work by Ofgem at the last price control review identified WPD as the best overall performer for network performance and we are pleased to be able to continue to demonstrate good restoration performance during harsh weather conditions. Ofgem has also recognised the wide gaps in performance between DNOs and acknowledged the severity of the targets set for WPD compared with the rest of the sector. We have agreed targets for the current five year period and are continuing to work with Ofgem to assist them in making comparisons between DNOs on an equitable basis.

Network performance (continued)

The WPD Group will continue with those initiatives that have clearly demonstrated good improvements to quality of supply to date, and will seek new opportunities and initiatives for the future. Our focus for 2008/09 and beyond will be to further reduce interruptions by progressing an ongoing programme to increase the automation of the HV network. Good progress was made during the year when a total of 62 new automation schemes were commissioned in WPD South Wales. This will ensure that, when an HV fault occurs, the maximum number of customers have their supplies restored within three minutes through automated sequence switching logic.

Customer service

We are committed to providing excellent customer service at all times and strongly believe that customer satisfaction is the key to the future success of the business. When dealing with customers our policy is to get it right "first time, every time". On the occasions when we fail to meet this standard, staff are encouraged to take personal responsibility for customer issues, to follow the problem through to the end, and to adopt our golden rule – "treat customers the way that we would like to be treated".

If customers are not happy with our efforts to resolve the matter, they may ask the independent consumer body *energywatch* to review their complaint. We have developed a good working partnership with *energywatch* to identify potential customer issues and resolve them before they develop into customer complaints. Regular meetings between WPD and *energywatch* have resulted in a number of initiatives to improve our overall service to customers and drive standards up.

This focus on customer service and the commitment our staff have shown in following the golden rule has enabled the WPD Group to reduce distribution complaints to Ofgem/*energywatch* substantially over the last nine years. In 2007/08, the WPD Group maintained its position as the best performing DNO in terms of the lowest number of complaints to *energywatch*. For the fifth year in succession, *energywatch* received no complaints in respect of WPD South Wales.

The introduction of the Consumers, Estate Agents and Redress ("CEAR") Act 2007 will result in closure of *energywatch* and this is scheduled to happen in October 2008. The CEAR Act also requires every network operator to become a member of an approved redress scheme. Customers may refer complaints to the scheme once the network operator has had an opportunity to resolve them, so that they are investigated and determined by an independent person. WPD joined The Energy Ombudsman, a service operated by The Ombudsman Service Limited, on a voluntary basis on 31 March 2008. The CEAR Act requires Ofgem to formally approve the scheme and we have been working with both the industry and Ofgem to develop an appropriate statutory scheme.

Ofgem also conducted a survey on the views of customers of the telephone response that they receive when they contact a DNO. Results published by Ofgem for the year show that the WPD Group performed above the national average. WPD South Wales was ranked second in the league table of all DNOs for the quality of its call centre performance. Ofgem also compared the speed of response that a DNO call centre provides and WPD was identified as a top performer with an average speed of response below 2 seconds compared to a national average of 42 seconds.

2 Operating and Financial Review for the year to 31 March 2008

Customer service (continued)

WPD's excellent customer service was further recognised when it was awarded a Charter Mark for a record fifth time in 2005. Charter Mark is the Government standard for customer service to the public and WPD is the only energy company to have held the Charter Mark continuously since its launch in 1992. The standard is now re-assessed annually to ensure ongoing compliance across each of the six different criteria which cover a total of 63 different categories of customer service. In 2007 WPD was found to have maintained its high standards across all of the criteria and, as a result, it has been confirmed that we will retain the Charter Mark for a further year. As part of the award process, WPD was also identified as best practice performer in ten categories. These are areas where we not only demonstrated that we met all the requirements, but that we had gone the extra mile to deliver a service identified as the best in its category. We are very proud of this achievement and regard it as another dimension to our continuing commitment to providing a high quality of customer service.

The Government has launched a re-branded scheme to replace Charter Mark - the “Customer Service Excellence Standard” - from April 2008 and WPD will make the transition to the new standard in 2009.

Capital investment

Gross capital investment (before customers' contributions) during the year was £92.6m across the WPD South Wales region and included the replacement of both overhead lines and switchgear together with the introduction of new technology.

A number of significant projects were tackled during the year:

- A £150,000 investment in the electricity infrastructure in Llandeilo town centre by WPD will improve services to customers and help safeguard supplies. The initiative involved laying and connecting new electricity mains cable and service connections to shops and homes, renewing over 300 metres of electricity cable along with 45 service connections to properties. The work was necessary because the existing electricity cables, which were installed in the 1950s, had become unreliable. WPD worked closely with the South Wales Trunk Road Agency and Carmarthenshire County Council in the planning and drawing up of an alternative traffic management system for Llandeilo to take into account necessary road closures during the period of work and to make sure that disruption to traders in this busy town was kept to a minimum.

- The South Hook project in West Wales is a small but significant step forward in helping to ensure that gas supplies entering the UK are secure in the medium to long term. WPD's part in this involved the establishment of a new 132/33 kV site at the South Hook terminal complex at Pembroke. The increased capacity will allow pumping of the raw imported liquid natural gas product to a site outside Swansea and on from there into the UK gas transmission network helping to secure future energy supplies for all UK customers.

- The Ammanford substation site is an important pivotal location for the supplies into the industrial location of Llanelli and provides a link into the 33kV system of West Wales via Carmarthen. The network has recently been upgraded and this included two new 132/33kV 60MVA grid transformers combined with a complete replacement of all the 33kV switchgear at the site. The completion of this scheme provides a sound basis for the wider 33kV network from Ammanford to Llanelli and beyond to operate reliably and efficiently for many years into the future. The scheme value was £1.2m.

Capital investment (continued)

- The south western area of Cardiff including the bay area and the political epicentre of Wales has seen significant development and growth due to inward investment. As a consequence the ageing infrastructure was reviewed and a scheme initiated to reinforce WPD’s Cardiff West bulk supply point with two new 132/33kV 90MVA grid transformers. These two new units now run in parallel with the site at Cardiff North providing 3 major in-feeds to the South West of Cardiff. The completion of this scheme combined with an extensive review and overlay of the older gas filled cables running between Cardiff West and Cardiff North (major grid sites) has ensured a safe, reliable and robust supply arrangement to the political and economic centre of Wales. The total scheme value was £1.7m.

- A project to instigate WPD's new data communications network, which includes the private mobile radio ("PMR") system, has made significant progress during the year. The new system, which is expected to be fully operational during 2008, will support not only voice communication but in the future will also have the flexibility to support both mobile ENMAC (WPD's network management system) as well as rural automation data. A programme to replace 1,450 handsets in WPD vehicles was completed in 2007 and, in addition to the new vehicle handsets, power supply upgrades and new aerial installations have now been completed at all 100 base stations across WPD. The base stations are scheduled for replacement in the first part of 2008 and will form phase 2 of this £5.0m project. Building the new network with the minimum of fuss and disruption to users was a major achievement and the system will form an integral part of WPD's reliable, resilient telecoms infrastructure.

Staff

The average number of employees during the year was 878 (2007: 958). These include a proportion of WPD South West staff who work in part for WPD South Wales. The reduction in numbers relates primarily to metering staff who transferred to a third party under the Transfer of Undertaking Protection of Employment Rights Act ("TUPE").

The WPD Group's policies on equal opportunities and employee consultation are set out within the Directors' Report (section 4). WPD believes that its relations with its employees are good.

2 Operating and Financial Review for the year to 31 March 2008

Regulatory issues

2007/08 was the third year of a five year price control period. In their final proposals, Ofgem confirmed that the RPI-X mechanism will apply and that X will be set at 0% with a one-off P0 increase in 2005/06 for WPD South Wales of +6.2%. The cost of capital has been set at 4.8% post-tax for the period. The final proposals, along with the detailed modifications to our distribution licence, were incorporated into our licence to take effect from 1 April 2005. Ofgem has recently confirmed that the RPI-X methodology will be continued into the next price control period which will run from 2010 to 2015.

In order to comply with the requirements of our licence and the Competition Act, the WPD Group continued with its compliance programme to ensure that all our policies and procedures meet the legal requirements. As part of the programme, all staff have received an updated code of conduct on fair competition.

During the sixth full year of Ofgem's IIS, the WPD Group believes it has, at a minimum, met its regulatory targets for each of the three key areas to which the incentive scheme applies, namely:

- the number of interruptions that customers experience;
- the duration of those interruptions; and
- the quality of telephone response from the distribution business to the customer.

As discussed previously, the incentive scheme can lead to an increase or a reduction in revenue of up to 3% depending on performance. Subject to confirmation of the declared year-end results by Ofgem's auditors, we have exceeded our targets for network performance and earned an income uplift for the year.

We have been set annual targets by Ofgem for customer minutes lost and customer interruptions for the current price control period which runs until March 2010.

Environment

The WPD Group is committed to conducting its business as a responsible steward of the environment. WPD plan new routes so as to minimise, as far as economically possible, their impact on the environment.

Every member of staff is made aware of WPD's environmental commitment to abide by environmental laws, regulations and corporate environmental policies, and their responsibilities for reporting any concerns on potential environmental compliance issues so that appropriate action can be taken.

WPD, which was the first DNO to gain independent accreditation (by Lloyds Register) against British Standard PAS55 - Asset Management, has successfully passed subsequent surveillance audits in 2007/08. Whilst an asset management specification, PAS55 encompasses risk management, setting of and adherence to policies and procedures, and thus has relevance to the control of environmental risk.

Fluid filled cables

The design of very high voltage underground cables has evolved over many years and our new cables all use a solid plastic like insulation. Old designs of 33kV and higher voltage cables used an insulating oil in ducts inside the cable. Whilst these cables are normally very reliable, in the event of a fault, or commonly damage by third parties digging the street, this oil may leak out, sometimes many hundreds of litres. In common with other UK distribution companies, WPD works to an operating code agreed with the Environment Agency ("EA"), and assesses both the condition and the environmental risk posed by the 214 km of fluid filled cables which WPD owns. The losses from WPD's fluid filled cables were low in 2007/08, and comprised a number of small leaks at disparate locations rather than high volume single events:

	Fluid losses (litres)
2005/06	2,689
2006/07	320
2007/08	662

At the start of 2008, WPD has initiated a regime of monthly leak reporting to the EA, following agreement in the joint EA and Energy Networks Association ("ENA") fluid filled cables group.

SF6 gas

Sulphur hexafluoride (SF6) is a manmade gas which has had widespread use such as in double glazing, tennis balls, training shoes as well as a number of industrial applications including high voltage switchgear. Unfortunately it is also a strong greenhouse gas, with a global warming potential 23,900 times greater than C02.

WPD carefully monitors its SF6 equipment and employs the ENA Engineering Recommendation S38 methodology for the reporting of SF6 banks, emissions and recoveries. That ENA document, drafted by WPD, employs approaches set out by The Intergovernmental Panel on Climate Change ("IPCC"), set up by the World Meteorological Organisation and the United Nations Environmental Programme.

WPD's losses from SF6 equipment in 2007/08 amounted to 209kg representing 0.89 % of its bank. The majority of this loss was due to leakage from older technology bulk 132kV SF6 circuit breakers on one site. These circuit breakers are of complex high pressure design and account for some 3,500kg of WPD's SF6 bank. During the year, WPD used specialist contractors to recover 143kg of SF6 from equipment being scrapped. It is proposed that future action on this equipment will be considered as part of the upcoming price review and stakeholder consultation process.

Environment (continued)

Electric and magnetic fields ("EMFs")

Concerns have been expressed by some members of the public regarding potential health effects of power frequency EMFs, which are emitted by all devices carrying electricity, including electric transmission and distribution lines and substation equipment. Government officials in the United States of America ("US") and the UK have reviewed this issue. The US National Institute of Environmental Health Sciences concluded in 2002 that, for most health outcomes, there is no evidence of EMFs causing adverse effects. The agency further noted that there is some epidemiological evidence of an association with childhood leukaemia, but that this evidence is difficult to interpret without supporting laboratory evidence. The UK National Radiological Protection Board (part of the UK Health Protection Agency) concluded in 2004 that, while the research on EMFs does not provide a basis to find that EMFs cause any illness, there is a basis to consider precautionary measures beyond existing exposure guidelines.

In April 2007, the Stakeholder Group on Extremely Low Frequency EMF, set up by the UK Government, issued its interim assessment which describes a number of options for reducing public exposure to EMFs. This assessment is being considered by the UK Government. PPL Corporation and its subsidiaries believe the current efforts to determine whether EMFs cause adverse health effects should continue and are taking steps to reduce EMFs, where practical, in the design of new transmission and distribution facilities.

General

WPD has continued its tree scheme for the sixteenth year, which is an integral part of its community support programme. Our partnerships with Silvanus Trust and the British Trust for Conservation Volunteers enable us to use local knowledge and experience. During 2007, 4,757 trees and shrubs were planted. WPD funding was also used for different projects such as the creation of orchards, wildlife areas, and tree nursery management.

To inform the Ofgem debate on sustainability and environmental impact issues on network losses from 11kV overhead lines, a research project has been initiated with Bath University to undertake a Life Cycle Assessment study. The work seeks to examine carbon/energy impacts of conductor sizing choice both at new build and on early intervention to save losses prior to the need to uprate for network capacity reasons. The work also considers the undergrounding of overhead lines.

Within WPD, recycling initiatives have included a move to use recycled paper amounting to some 26 tonnes per year and recycling of more than 700kg of soft drinks cans. WPD sponsored the annual summer show at Cardiff's hands on science centre, Techniquest. The 2007 show was all about recycling and aimed to provide families with lots of practical advice and tips on how they can recycle. It was entitled "Gran Designs" and featured an eccentric grandmother and her two young grandchildren as they come up with weird and wonderful ways to conserve energy and do their bit for the planet.

Insurance arrangements

The WPD Group has a wholly-owned captive insurance company, Aztec Insurance Limited ("Aztec"), based in Guernsey. Depending on the nature of the risk, WPD South Wales carries all or an element of the risk itself ("self insured") or it underwrites insurance with a combination of Aztec and external insurers.

Insurance arrangements in place as at 31 March 2008 relating to the WPD Group's key risks were as follows:

- the distribution network is self insured.

- offices and depots including their contents and stock are self insured up to £500,000 for each claim and externally insured above that, subject to an annual maximum of £50.0m.

- combined liability covers employers' liability, public and product liability, and professional indemnity. The first £10,000 of each claim is self insured, Aztec cover the next £1.0m of any claim up to a maximum of £3.5m in any one year, and the excess is externally insured subject to certain limits.

- on motor related claims, damage to own vehicles is self insured, as is the first £5,000 of each third party claim. Any excess is covered by Aztec up to a maximum of £1.0m for any claim and £1.25m in aggregate; beyond that is externally insured subject to certain limits.

- claims relating to death or injury to employees whilst on WPD business or travelling on business is externally insured subject to various limits.

- external insurance is also in place (subject to limits) for loss of money, securities or property through dishonest acts by employees and for wrongful acts by pension scheme trustees. Insurance in respect of directors and officers is maintained by the WPD Group's US parent, PPL Corporation.

Insurance arrangements are reviewed in detail annually.

2 Operating and Financial Review for the year to 31 March 2008

Treasury related matters

Risk management
The WPD Group does not undertake transactions in financial derivative instruments for speculative purposes. The Group's debt is substantially long term and at fixed interest rates thus limiting exposure to interest rate fluctuations. All debt at WPD South Wales is denominated in sterling and therefore there is no currency risk exposure.

Credit rate risk
Both WPD South Wales and WPD South West are required by their distribution licences to maintain investment grade ratings, which they have done. WPD South Wales and WPD South West both have the following long-term corporate credit ratings: Fitch BBB+ and Standard & Poor's BBB+.

Any cash deposits are only made by the Group to third parties with a high credit rating and within strict limits imposed by the Board.

Liquidity
On a day-to-day basis, WPD South West provides liquidity to the WPD Group. It has borrowing arrangements in place with a range of third parties with high credit ratings. At 31 March 2008, WPD South West had a £150m undrawn five-year committed borrowing facility that expires in October 2009 of which all conditions precedent had been met at that date. WPD South West also had undrawn uncommitted facilities of £65.0m. In addition, at 31 March 2008 the WPD Group's parent Western Power Distribution Holdings Limited ('WPDHL') has a £150m undrawn committed borrowing facility that expires in January 2013 of which all conditions precedent had been met at that date; this facility may be extended by one year through an option exercisable in January 2009.

WPD South Wales debt
At 31 March 2008, WPD South Wales had £366.9m (£2007: £366.6m) of external debt outstanding as shown on its balance sheet with £150m nominal maturing in 2020 and £225m nominal maturing in 2037.

£50.0m 7% cumulative preference shares are held by another WPD Group company (31 March 2007: £50.0m). These preference shares are classified as liabilities as opposed to equity.

At 31 March 2008 and excluding the preference shares, WPD South Wales was owed net £299.8m by other WPD Group companies (31 March 2007: £263.7m).

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

The Memorandum and Articles of Association of the WPD Group's parent, WPDHL, place restrictions on dividends or other value which can be paid to the WPD Group's owners. An independent director has been appointed to oversee this: he in turn may seek financial advice from an independent expert. No payment or transfer of value can be made without the independent director first certifying that certain financial tests have been met.

In 2007/08, dividends paid by WPD South Wales comprised £6.0m (2007: £48.0m) on equity shares.

2 Operating and Financial Review for the year to 31 March 2008

Regulatory Financial Statements

The Regulatory Financial Statements within this document are prepared in a format which closely follows that which would apply for statutory accounts.

Profit and loss account (Section 6.3)
Profit before tax for 2007/08 was £82.2m compared with £79.8m for the previous year, an increase of £2.4m. Turnover fell by £1.8m. Operating expenses were £2.1m lower. Cost of sales fell by £2.2m due to lower levels of rechargeable engineering work. The depreciation charge (including losses on disposal) fell by £10.2m largely as a result of an increase in the assumed lives of network assets effective from 1 April 2007. Underlying operating expenses excluding depreciation and cost of sales increased by £10.3m which largely related to pension costs. Net interest expense fell by £2.1m due to lower average debt.

The tax charge has increased by £16.7m compared with 2006/07; this is explained within 'Taxation' below.

Balance sheet (Section 6.5)
Total net assets at 31 March 2008 were £537.8m, an increase of £55.3m on the previous year. Fixed assets increased by £42.1m reflecting the fact that capital expenditure exceeds the historical cost depreciation charge. The deferred tax provision (other than that on the pension liability) fell by £5.6m.

Cash flow statement (Section 6.6)
There was a cash inflow before financing activities of £30.9m compared with a cash outflow of £35.8m in the previous year. The cash inflow from operating activities was £112.8m compared with £126.3m the previous year. Net interest paid increased by £5.6m, largely due to the payment of £7.0m in preference dividends to another Group company (2007: nil). There were no tax payments in the current year compared with net payments totalling £46.1m in the previous year, which largely reflects the timing of payments made to other WPD Group companies for group relief. Net capital expenditure was £2.3m higher. Equity dividends paid fell by £42.0m; these are used largely to settle interest on external borrowings by other companies in the Group.

Taxation

An analysis of the tax charge is given in Note 6 to the Regulatory Financial Statements. The overall tax charge has increased by £16.7m from £1.0m in 2007 to £17.7m in 2008. Of the increase, £5.4m is within current tax and £11.3m within deferred tax.

Current tax
The increase in the current tax charge in 2008 over that in 2007 is due to a higher profit before tax in 2008 and a reduction in favourable prior year adjustments.

Current tax was provided at a rate less than the current rate of corporation tax of 30% due to the surrender of tax losses from other WPD Group companies at less than the standard rate. The Company intends to continue to utilise tax losses available in other WPD Group companies to offset its tax liability in whole or in part.

Taxation (continued)

Deferred tax

Deferred tax is provided for under Financial Reporting Standard 19 ("FRS19") "Deferred tax"'. This recognises the timing differences between the accounting and tax treatment of certain categories of expenditure, both capital and revenue. The main element of the provision relates to the differences between depreciation charged in the accounts and the tax allowances applicable to that expenditure. WPD has adopted the policy of discounting allowable under FRS19. Deferred tax was favourably impacted in 2007 by £21.6m as a result of an increase in the discount following an increase in the interest rate used; in 2008, there was an adverse impact of £4.4m primarily as a result of the change in assumed asset lives (Note 11). Following the change in the rate of corporation tax to 28% effective 1 April 2008, deferred tax was reduced by £9.1m.

Effective rate

The effective tax rate is the implied rate shown by dividing the tax charge in the profit and loss account by the profit on ordinary activities before tax as shown in that statement. For 2008, this was 22% for WPD South Wales (2007: 1%). For 2008, this is lower than would have been expected mainly due to the impact of the rate reduction on deferred tax. For 2007, the effective rate was 1% mainly due to an increase in the deferred tax discount.

Principal risks and uncertainties

Regulatory risk

The substantial part of the Company's revenue is regulated and is subject to a review every five years. The current review period ends on 31 March 2010.

Under the review, Ofgem assesses the revenue and capital expenditure plans of the Company and determines what they consider an efficient level of that expenditure. Ofgem also considers the required cost of capital sufficient to encourage the required investment in the network, and determines customer service targets.

The Company's management invests considerable resources in the review process and has been proactive in working with Ofgem to establish better measures of cost recording to inform future reviews.

If the Company feels that, as a result of a review it would financially be unable to continue to operate and to meet its obligations under the licence, then it has the right to refer the matter to the Competition Commission for a determination.

Network disruption

Disruption to the network could reduce profitability both directly through the lower units delivered on which income is charged, and also through the system of penalties and rewards that Ofgem has in place relating to customer service levels (discussed under 'Network performance' above).

There are economic restrictions on the level of capital expenditure that can be incurred to make the network totally reliable. A certain level of risk must be accepted and this is recognised by Ofgem in its regulatory review. However, the Company believes that its network is robust. It targets capital expenditure on schemes which are assessed to have the greatest improvement in customer service levels. It also spends considerable sums on routine maintenance, including tree cutting to keep trees away from lines both for safety reasons and as trees have been proven to be a major cause of network interruptions. The Company has met Ofgem's targets for customer service.

2 Operating and Financial Review for the year to 31 March 2008

Principal risks and uncertainties (continued)

Environment
Certain environmental issues are discussed above. There is always the risk that changes in legislation, including those imposed on the UK by the European Union, could result in considerable costs being incurred by the Company with no guarantee that Ofgem would allow them to be recovered through regulated income.

Treasury
The risks associated with the treasury activity, including the ability to raise funding to meet the Company's capital expenditure programme, are discussed in the 'Treasury related matters' section above.

Financial
Risks associated with financial processes are discussed in Section 3 'Corporate Governance'.

Pensions
Most of the employees are members of a defined benefit pension scheme, which also has a considerable number of members who are either retired or have deferred benefits. There are risks associated with the financial performance of the assets within the scheme and with the estimate of the liabilities of the scheme including longevity of members. Currently, ongoing service costs and a proportion of the deficit costs are recoverable through the regulated income.

3 Corporate Governance

The Company is committed to the highest standards of corporate governance.

The Company is indirectly owned by one corporate shareholder and thus many of the specific requirements of the Listing Rules of the Financial Services Authority are not applicable to the Company. The corporate shareholder is PPL Corporation ("PPL" - see Section 4).

Board of directors

The Board of the Company comprises three executive directors and one non-executive director. Details of the Board members are set out in the Directors' Report within Section 4.

The Board of the Company has reserved certain matters for itself to approve. It has also set out a framework of authority levels within which the executive directors may operate. In addition, the WPD Group's executive directors, non-executive directors and other shareholder representatives informally discuss the Company's operations on a regular basis.

The Board of Western Power Distribution Holdings Limited ("WPDHL"), the holding company for the WPD group, meets formally at least four times per annum. The Chairman is appointed by PPL. This Board also has an independent director as a member; he has responsibilities under that company's constitution relating to the ability of that company to transfer value to other PPL group members, such as the declaration of a dividend.

WPD's executive directors together with senior managers at PPL receive a detailed monthly group financial report. In addition, WPD's executive directors formally report both financial and non-financial performance at the WPDHL Board meetings.

Board committees

Due to the nature of the ownership of the Company, there are no requirements for formal Nomination and Remuneration Committees. In particular, executive directors' remuneration has been set directly by PPL. The WPD Group's operations are subject to internal audit examination and the results reported to both the WPDHL Board and to PPL's Audit Committee.

The responsibility for audit is assumed by the Board as opposed to being delegated to a sub committee. As set out below, copies of all WPD Corporate Audit reports were submitted to the General Manager of PPL Corporate Audit Services at PPL during the year.

The Executive Committee comprises the executive directors and meets on a monthly basis. Matters requiring disclosure to the Board are defined within the Company's Constitution and Authorities document. The Company Secretary ensures that all relevant items are disclosed.

3 Corporate Governance (continued)

Internal control environment

The directors of WPD have overall responsibility for the system of internal controls and for reviewing the effectiveness of the system. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives. In pursuing these objectives, internal control can only provide reasonable and not absolute assurance against material mis-statement or loss.

There are many cultural features in WPD that contribute directly to the success of the Company and the results that it has achieved. These include:

- good definition and communication of short-term business objectives and targets.
- commitment to achievement of objectives and targets.
- speedy decision-making.
- business environment that empowers managers.
- an uncomplicated management structure that aids the flow of information both ways through the organisation.

In order for this success to occur, the control environment is one which empowers those with direct responsibility to take decisions within a clearly defined control framework. The control mechanisms have to be sufficient to limit risk but appropriate to the Company's ability to react quickly and effectively to events, therefore enabling the Company to deliver results over a sustained period of time.

It is important for an organisation to have a clearly defined structure of control expectations. The controls start at director level and make it clear to everyone concerned how the business should be conducted (policy) and how far each person can go in conducting that business (authority levels). This information is communicated effectively to all levels of staff.

As the WPD Group is owned by a US publicly quoted company, it is subject to the requirements of the 2002 US Sarbanes-Oxley Act. Section 404 of this Act details the requirement for the organisation to demonstrate that good internal controls exist around financial reporting. WPD comply with these requirements via a two stage approach.

Firstly, Company level controls which are pervasive across the Company are documented and tested. The controls cover the COSO elements of effective internal control which encompass:

- control environment
- risk assessment
- information and communication
- control activities
- monitoring.

Secondly, all the major financial processes have been documented with specific detail on the controls in place. Management monitor and test these controls on an ongoing basis. In addition, the controls are reviewed by the Internal Audit department and any issues identified and communicated back to management and the process owners to enable improvement to the controls. In the year to December 2007, WPD's compliance with the Act was also reviewed in detail by the WPD Group's external auditors. Good controls together with appropriate documentation must be maintained, and this is subject to testing by management and both internal and external auditors on an annual basis. Since inception of the Act, no significant deficiencies nor material weaknesses have been identified in WPD's financial control environment.

3 Corporate Governance (continued)

Identification and evaluation of risks and control objectives

The Company's strategy is to follow an appropriate risk policy, which effectively manages exposures related to the achievement of business objectives.

Key stakeholders are responsible for identifying and assessing the key business risks associated with achieving the corporate objectives. Any actions required to further enhance the control environment are identified along with the person responsible for the management of the specific risk. Periodically a review of key risks is undertaken from which an operational plan is created and used by Internal Audit to assess the risks and the appropriateness of the controls which are in place to manage the risk. The progression of this operational plan is communicated to the owners on a quarterly basis as are all key observations. This method encourages the key stakeholders to actively manage the risks within their areas on a proactive basis.

The Internal Audit and Business Controls department helps to ensure that the risk management and internal control system is consistently adopted, updated and embedded into the business processes.

Individual risk assessment reports highlight the most significant risks affecting the business process, the actions being taken to mitigate these, and also ensures that individuals are responsible for the management of these risks. This information is provided to the Board, the US owner's audit department, and also the external auditors.

A risk management methodology has been produced and shared with the senior management team in order to ensure a consistent and co-ordinated approach to risk management is undertaken within the business. This methodology is available to all staff within the corporate electronic library.

Auditor independence

As mentioned above, PPL is subject to the US Sarbanes-Oxley Act. This Act not only requires documentation and review of internal controls but also details how audit committees, management, and auditors carry out their respective responsibilities and interact with each other. Its purpose is to build and restore confidence in public financial reporting within the US. The Act lays out specific requirements for each of these parties as it relates to corporate responsibilities, auditor regulation and independence, and financial reporting.

As a wholly owned entity of PPL, the requirements of the Sarbanes-Oxley Act extend to WPD. One of the main elements of the Act is concerned with registered public auditing firms being unable to undertake non-auditing services if they are performing auditing services for the group. However a public accounting firm may engage in non-audit services, including tax services, for an audit client, but only if the activity is approved in advance (pre-approved) by the audit committee of the parent company. Therefore any non-auditing services required by WPD, other than those regarded as de-minimis, are detailed to PPL in advance and require their approval.

PPL has adopted a policy of tendering for its world-wide audit services at least every seven years. This is to ensure that best practice is followed in relation to corporate governance and that fees are competitive. Following a tender exercise during 2005, PPL selected Ernst & Young LLP to replace PricewaterhouseCoopers LLP during 2006 for their various world-wide audits.

3 Corporate Governance (continued)

Code of Ethics and Legal Compliance Statement

WPD has developed a formal "Code of Ethics" that defines the standards of personal behaviour to which individual Board members and all employees are required to subscribe. This is subject to annual revision and frequent communication to all employees.

Similarly, WPD has a "Legal Compliance Programme – Statement of Policy" which is also issued periodically to employees. This states that WPD "is dedicated to conducting its business with honesty, integrity and fairness". It also states that WPD will not tolerate retaliation against any employee who reports any illegal act by the Company or by a fellow employee. Any such reports may be made to a line manager or to a named Compliance Office within Human Resources, and may be made anonymously.

Code of conduct on fair competition

To ensure that the Company complies with it's Distribution Licence and the Competition Act 1998, WPD has issued a "Code of conduct on fair competition". This has recently been updated and reissued to all staff; a copy is given to all new employees. It also applies to agents who work for WPD.

Political donations and expenditure

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

4 Directors' Report

Principal activities

WPD South Wales' principal activity is the distribution of electricity. Distribution involves the delivery of electricity across the distribution network within its authorised area covering South Wales. The management of the WPD Group is involved in the management of the network in both South Wales and South West England, and where appropriate the South Wales and South West networks share engineering control and other systems.

Ownership

WPD South Wales is an indirect, wholly-owned subsidiary of Western Power Distribution Holdings Limited which is owned by PPL Corporation, an electricity utility of Allentown, Pennsylvania, US.

Business review

This is contained in Section 2 to this document.

Results and dividends

The profit for the financial year 2008 was £64.5m (2007: £78.8m). Profit on ordinary activities before tax is £82.2m (2007: £79.8m).

Dividends paid by the Company on equity shares totalled £6.0m (2007: £48.0m) during the year. The WPD Group is structured such that much of the debt outstanding is owed by a holding company. Dividend payments from the Company include those used to enable the holding company to make interest payments.

Payment of creditors

The WPD Group's policy in respect of its suppliers (other than those providing electricity utility supplies and services) is to require suppliers to accept our terms which are displayed on our official orders unless alternative terms of mutual benefit can be agreed. The average length of time for the payment of creditors during the year was 15 days (2007: 17 days).

Charitable donations

During the year ended 31 March 2008, donations of £42,000 were made by the Company to community organisations of which £5,000 was donated to charities. In addition, WPD South West established a charitable foundation in 1996 with a £1.0m donation and, in May 2001, an affiliate donated a further £1.0m to the foundation. The foundation made donations of £11,000 to organisations in South Wales in 2007/08.

4 Directors' Report (continued)

Political donations and expenditure

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

Equal opportunities

The WPD Group is committed to equality of opportunity in employment and this is reflected in its equal opportunities policy and employment practices. Employees are selected, treated, and promoted according to their abilities and merits and to the requirements of the job. Applications for employment by people with disabilities are fully considered, and in the event of members of staff becoming disabled, every effort is made to ensure that their employment with the WPD Group continues with redeployment or retraining arranged as appropriate. It is the policy of the WPD Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Employee consultation

The WPD Group places considerable value on the involvement of its employees in its affairs. Staff are kept informed of the WPD Group's aims, objectives, performance and plans, and their effect on them as employees through newsletters, regular team briefings and other meetings, as well as through the WPD Group's in-house journal. Formal meetings are held regularly between senior managers and representatives of staff and their unions to discuss matters of common interest. A series of road show presentations by the directors each year ensure that all staff are aware of, and can contribute to, WPD's corporate goals.

Directors and their interests

The directors who served during the year were as follows:

	Appointed
RA Symons, Chief Executive	15 September 2000
DCS Oosthuizen, Finance Director	4 January 2001
DG Harris, Resources and External Affairs Director	1 April 2004
RL Klingensmith, non-executive director and President PPL Global	14 February 2007

During and at the end of the financial year, no director was materially interested in any contract of significance in relation to the Company's business.

Insurance in respect of directors and officers is maintained by the WPD Group parent, PPL Corporation. The insurance is subject to the conditions set out in the companies acts and remains in force at the date of signing the Regulatory Financial Statements.

4 Directors' Report (continued)

Statement of disclosure to auditors

In the case of each of the persons who were directors at the time when the report is approved under Section 234A of the Companies Act the following applies:

(a) so far as the directors are aware, there is no relevant audit information of which the Company's auditors are unaware, and

(b) the directors have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of this information.

Auditors

Ernst & Young LLP have expressed their willingness to continue in office and a resolution proposing their re-appointment will be put before the Annual General Meeting.

5 Statement on link between directors' pay and performance

Introduction

The directors' bonus arrangement includes both financial and non financial performance criteria. Set out below are the non financial criteria relating to customer service and network performance.

The executive directors' bonus arrangements contain a substantial incentive to maintain and improve customer service and network reliability standards as well as ensuring that safety levels are maintained:

- goals for each element of performance are determined by the owner (PPL) at the beginning of each calendar year, specifying target and maximum goals together with associated target and maximum bonus amounts;

- following the end of the calendar year, results are compared with the goals, with the maximum amount paid if the maximum goals are met or exceeded; one half of the maximum if the target goals are met; or no payment if the target goals are not met.

Bonus payments are made annually based on a calendar year, with payment usually in the March following the calendar year end.

Year to 31 December 2007 goals

For the calendar year 2007, set out below are the maximum bonus amounts related to standards of performance included in the annual bonus programme as determined at the beginning of the year:

	Maximum Bonus Amount (% of base pay)		
	Chief Executive	Finance Director	Resources and External Affairs Director
Standard of performance goal:			
Network reliability			
Minutes lost per customer	9.00%	8.00%	7.00%
Customer interruptions	6.75%	6.00%	5.25%
Customer impact	6.75%	6.00%	5.25%
Contact Centre performance			
Total	**22.50%**	**20.00%**	**17.50%**

The above relates to the WPD Group as a whole.

Note:
(i) 'Minutes lost per customer' and 'customer interruptions' are defined as per Ofgem's Information and Incentives Scheme ("IIS") definitions.

(ii) 'Contact Centre performance' relates to the time taken to answer telephone calls from customers who have lost supply.

5 Statement on link between directors' pay and performance (continued)

Year to 31 December 2007 results

WPD’s results in 2007 not only met or exceeded all of Ofgem's IIS targets (on a pro rata basis for the calendar year) but also met or exceeded WPD’s maximum goals specified for these standards. Also, the Company achieved its highest level target of answering within 20 seconds at least 98% of calls from customers who had lost supply.

Accordingly the annual bonus payment made in March 2008 to each director in respect of 2007 performance included the maximum amounts for standards of service as specified in the above table.

2008 Goals

The same basic bonus structure has been retained in the 2008 annual bonus programme for each director.

6.1 Statement of directors' responsibilities in respect of the Regulatory Financial Statements

Each DNO is a natural monopoly regulated by Ofgem. It is therefore subject to control on the prices it can charge and the quality of supply it must provide. The principal legislation governing the structure of the electricity industry in Great Britain is the Electricity Act 1989, as amended by the Utilities Act 2000 and the Energy Act 2004. This legislation provides for a licence framework in which the operations of the DNOs are regulated, pursuant to which income generated is subject to an allowed revenue regulatory framework that provides economic incentives to minimise operating, capital and financing costs consistent with the DNOs providing an acceptably reliable distribution network and meeting their legal responsibilities. This licence framework is overseen by Ofgem.

Licences which govern DNOs require each DNO to produce regulatory accounts. One of the documents which comprise the regulatory accounts is the Regulatory Financial Statements. This document contains the Regulatory Financial Statements, which are subject to audit.

The Regulatory Financial Statements are prepared on a similar basis to financial statements which a company is required to produce under UK generally accepted accounting practice. This requires the directors to prepare financial statements for each financial year which fairly present the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently:
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors confirm that they have complied with the above requirements in preparing the Regulatory Financial Statements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

6.2 Independent auditors' report to the Director General of the Gas and Electricity Markets Authority (the "Regulator") and to Western Power Distribution (South Wales) plc

We have audited the Regulatory Financial Statements for the year ended 31 March 2008 which comprise the profit and loss account, the statement of total recognised gains and losses, the balance sheet, the statement of cash flows and notes to the statement of cash flows A to C, and the related notes 1 to 22.

This report is made, on terms that have been agreed, solely with the Company and the Regulator in order to meet the requirements of the regulatory licence. Our audit work has been undertaken so that we might state to the Company and the Regulator those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under the regulatory licence to procure such a report and (b) to facilitate the carrying out by the Regulator of its regulatory functions, 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 Regulator, for our audit work, for this report or for the opinions we have formed.

Basis of preparation

The Regulatory Financial Statements have been prepared under the historical cost convention, as modified by the revaluation of derivative financial instruments, and in accordance with Condition 42 of the Company's regulatory licence and the accounting policies set out in Note 1.

The Regulatory Financial Statements are separate from the statutory financial statements of the Company.

Respective responsibilities of the Regulator, the directors and auditors

The nature, form and content of the Regulatory Financial Statements are determined by the Regulator. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the Regulator's purposes. Accordingly we make no such assessment.

The directors' responsibilities for preparing the Regulatory Financial Statements in accordance with Condition 42 of the regulatory licence are set out in the Statement of directors' responsibilities in respect of the Regulatory Financial Statements.

Our responsibility is to audit the Regulatory Financial Statements having regard to the guidance contained in Audit 05/03 '*Reporting to Regulators of Regulated Entities*'.

We report our opinion as to whether the Regulatory Financial Statements present fairly, in accordance with Condition 42 of the Company's regulatory licence and the accounting policies set out in Note 1, the results and financial position of the Company. We also report to you if, in our opinion, the Company has not kept proper accounting records or if we have not received all the information and explanations we require for our audit.

We read the other information contained within the Regulatory Financial Statements, including any supplementary schedules on which we do not express an audit opinion, and consider the implications for our report if we become aware of any apparent mis-statements or material inconsistencies with the Regulatory Financial Statements. The other information comprises only the foreword, the operating and financial review, the corporate governance statement, the directors' report, and the statement on link between directors' pay and standards of performance.

6.2 Independent auditors' report to the Director General of the Gas and Electricity Markets Authority (the "Regulator") and to Western Power Distribution (South Wales) plc (continued)

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board except as noted below. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Regulatory Financial Statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the Regulatory Financial Statements, and of whether the accounting policies are consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Regulatory Financial Statements are free from material mis-statement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Regulatory Financial Statements are determined by the Regulator, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK and Ireland).

Our opinion on the Regulatory Financial Statements is separate from our opinion on the statutory accounts of the Company on which we reported on July 2008, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the Company (our "Statutory" audit) was made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a Statutory auditor's report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the Company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

Opinion

In our opinion the Regulatory Financial Statements fairly present, in accordance with Condition 42 of the Company's regulatory licence and the accounting policies set out in Note 1, the state of the Company's affairs at 31 March 2008 and of its profit and cashflow for the year then ended, and have been properly prepared in accordance with that condition and those accounting policies.

Ernst & Young LLP
Registered Auditor
Bristol

July 2008

6.3 Profit and loss account

For the year ended 31 March 2008

	Note	**2008** **£m**	2007 £m
Turnover	2	**184.8**	186.6
Operating expenses	3	**(96.0)**	(98.1)
Operating profit	3	**88.8**	88.5
Profit on sale of fixed assets		**0.1**	-
Profit on ordinary activities before interest and tax		**88.9**	88.5
Interest expense (net)	4	**(6.8)**	(8.9)
Other finance income	5	**0.1**	0.2
Profit on ordinary activities before tax	2	**82.2**	79.8
Tax on profit on ordinary activities	6	**(17.7)**	(1.0)
Profit for the financial year		**64.5**	78.8

All activities relate to continuing operations.

There is no difference between the profit on ordinary activities before tax and the profit for the financial year stated above, and their historical cost equivalents.

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

6.4 Statement of total recognised gains and losses

For the year ended 31 March 2008

	Note	**2008** **£m**	2007 £m
Profit for the financial year		**64.5**	78.8
Actuarial gain/(loss) recognised in the Infralec 92 pension scheme	9(d)	**0.7**	(0.6)
Movement on deferred tax relating to the Infralec 92 pension scheme		**(0.2)**	0.2
Actuarial gain/(loss) recognised in the WPUPS pension scheme	9(e)	**8.9**	(14.7)
Movement recognised on WPUPS reimbursement agreement	9(e)	**(8.9)**	14.7
Movement on deferred tax relating to the WPUPS pension scheme		**(3.5)**	4.4
Movement on hedging reserve (net of tax)	19	**(0.2)**	3.1
Total recognised gains and losses for the year		**61.3**	85.9

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

6.5 Balance sheet

31 March 2008

	Note	**2008 £m**	2007 £m
Fixed assets			
Tangible assets	11	**755.7**	713.6
		755.7	713.6
Current assets			
Stocks	12	**0.9**	1.9
Debtors	13		
Amounts falling due within one year		**403.8**	404.4
Amounts falling due after one year		**9.0**	30.0
		413.7	436.3
Creditors			
Amounts falling due within one year	14	**(141.3)**	(158.9)
Net current assets		**272.4**	277.4
Total assets less current liabilities		**1,028.1**	991.0
Creditors			
Amounts falling due after more than one year	14	**(416.9)**	(416.6)
Provisions for liabilities and charges	15	**(62.3)**	(67.9)
Net assets excluding pension liability		**548.9**	506.5
Pension liability (net of tax)	9	**(11.1)**	(24.0)
Net assets including pension liability		**537.8**	482.5
Capital and reserves			
Called-up share capital	17	**201.7**	201.7
Share premium account	19	**23.2**	23.2
Capital redemption reserve	19	**5.1**	5.1
Hedging reserve	19	**9.3**	9.5
Profit and loss account	19	**298.5**	243.0
Total shareholders' funds	18	**537.8**	482.5

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

The Regulatory Financial Statements on pages 29 to 57 were approved by the Board of Directors on 18 July 2008 and were signed on its behalf by:

RA Symons
Chief Executive

DCS Oosthuizen
Finance Director

6.6 Statement of cash flows

For the year ended 31 March 2008

	Cash flow note	**£m**	**2008 £m**	£m	2007 £m
Net cash inflow from operating activities	A		**112.8**		126.3
Returns on investments and servicing of finance					
Interest received		**19.4**		0.2	
Interest paid		**(24.8)**		(14.0)	
Proceeds on termination of interest rate swaps		**-**		13.9	
Issue costs on new long-term loans		**(0.1)**		(7.0)	
Preference share dividends paid to shareholders		**(7.0)**		-	
Net cash outflow from returns on investments and servicing of finance			**(12.5)**		(6.9)
Taxation					
Group relief paid		**-**		(46.8)	
Refund received		**-**		0.7	
Net cash outflow from taxation			**-**		(46.1)
Capital expenditure and financial investment					
Purchase of tangible fixed assets		**(90.2)**		(81.7)	
Customers' contributions received		**26.6**		20.6	
Sale of tangible fixed assets		**0.2**		-	
Net cash outflow from capital expenditure and financial investment			**(63.4)**		(61.1)
Equity dividends paid			**(6.0)**		(48.0)
Cash inflow/(outflow) before financing			**30.9**		(35.8)
Financing					
New long-term loans		**-**		225.0	
Movement in balances with Group undertakings		**(30.9)**		(189.2)	
Net cash (outflow)/inflow from financing			**(30.9)**		35.8
Movement in cash in the year	B, C		**-**		-

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

6.6 Notes to the statement of cash flows

For the year ended 31 March 2008

A. Reconciliation of operating profit to net cash inflow from operating activities

	2008	2007
	£m	£m
Operating profit	**88.8**	88.5
Depreciation	**22.7**	31.5
Loss on disposal of tangible fixed assets	**-**	1.4
Decrease in stocks	**1.0**	0.9
Decrease in debtors	**3.2**	1.7
(Decrease)/increase in creditors	**(2.6)**	3.1
Decrease in provisions	**-**	(0.3)
Difference between pension charge and cash contributions	**(0.3)**	(0.5)
Net cash inflow from operating activities	**112.8**	126.3

B. Analysis of changes in net debt

	At 1 April 2007	Cash flow	Other non-cash movements	**At 31 March 2008**
	£m	£m	£m	**£m**
Debt due after one year :				
£150m 9.25% Eurobonds 2020	(148.6)	-	(0.1)	**(148.7)**
£225m 4.804% bonds 2037	(218.0)	-	(0.2)	**(218.2)**
7% preference shares issued to a Group undertaking	(50.0)	-	-	**(50.0)**
Other balances with Group undertakings	263.7	30.9	5.2	**299.8**
	(152.9)	30.9	4.9	**(117.1)**

C . Reconciliation of net cash flow to movement in net debt

	2008	2007
	£m	£m
Issue of external debt (net of issue costs)	**-**	(218.0)
Change in balances with Group undertakings:		
Non-cash changes	**5.2**	7.7
Cash flow changes	**30.9**	189.2
Amortisation of finance costs	**(0.3)**	(0.1)
Decrease/(increase) in net debt in year	**35.8**	(21.2)
Net debt at 1 April	**(152.9)**	(131.7)
Net debt at 31 March	**(117.1)**	(152.9)

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

1. Accounting policies

The principal accounting policies are summarised below.

Basis of preparation

The Regulatory Financial Statements have been prepared on the going concern basis under the historical cost convention, as modified by the revaluation of derivative financial instruments, and in accordance with the Companies Act 1985 and applicable accounting standards. Accounting policies are prepared under United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). They have been applied consistently throughout the year and the preceding year except where changes have been made to previous policies on adoption of new accounting standards.

Changes in accounting policy

Financial Reporting Standard ("FRS") 29 'Financial Instruments: Disclosures' is applicable to the Company for the year ended 31 March 2008. The Company has taken advantage of the exemption in FRS 29 from presenting FRS 29 disclosures, as full equivalent disclosures are presented on a Group basis within the consolidated financial statements.

Turnover

Turnover is stated net of value added tax. Sales relating to electricity distributed during the year include an estimate of the sales value of units distributed to customers but not billed by the year end. Remaining sales relate to the invoice value of other goods and services provided.

IT consultancy and software development costs

Significant IT consultancy and software development costs are capitalised when tangible benefits accrue and are amortised over their estimated useful economic life from the date of first use. Costs primarily relate to external suppliers; directly attributable internal costs are capitalised only if significant. Other IT consultancy and development costs are charged to the profit and loss account in the year in which they are incurred.

Research

Expenditure on research is written off to the profit and loss account in the year in which it is incurred.

Pension costs

The Company participates in three defined benefit pension schemes:

- the Electricity Supply Pension Scheme ("ESPS"), to which most employees in the Group belong. Under the guidance of FRS 17 "Retirement Benefits", where an entity cannot separate out its share of the scheme's assets and liabilities on a reasonable and consistent basis, the relevant entity should account for pensions as if the scheme were a defined contribution scheme, and charge contributions to the profit and loss account and capital expenditure as they become payable in accordance with the rules of the scheme. This applies in these Regulatory Financial Statements.

- the Infralec 1992 Pensions Scheme ("Infralec 92"). The Infralec 92 provides benefits on both a money purchase and final salary basis and is operated by WPD South Wales.

- the Western Power Utilities Pension Scheme ("WPUPS"). However, another WPD Group company, Western Power Distribution Holdings Limited, has accepted responsibility for liabilities for WPUPS and reimburses all contributions made by the Company. The liability under FRS 17 in respect of WPUPS recorded in these Regulatory Financial Statements is offset by the reimbursement agreement.

Any capital cost of ex gratia and supplementary pensions, including early retirement deficiency contributions, are charged to the profit and loss account when the contribution is paid to the pension scheme.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

1. Accounting policies (continued)

Share based payments

The Company operates a phantom share option scheme for executive directors and senior managers. Options are valued using the Black-Scholes option-pricing model. No performance conditions are included in the fair value calculations. The expected volatility is based on historical volatility over the last three years. The expected life is the average expected period to exercise. The risk free rate of return is based on US Treasury bonds available at the date of grant and of a similar duration.

Leases

Rentals for operating leases are charged to the profit and loss account in equal annual amounts over the period of the lease.

Interest costs

Interest costs of debt are recognised in the profit and loss account over the term of such instruments at a constant rate on the carrying amount.

Tangible fixed assets

Tangible fixed assets are stated at cost net of customer contributions, less amounts provided to write off the cost less anticipated residual value of the assets over their useful economic lives, which are as follows:

	Years
Distribution network assets:	
Overhead lines and poles	45
Underground cables	60
Plant and machinery (transformers and switchgear)	45
Meters	Up to 19
Customer contributions	55
Other (towers and substation buildings)	Up to 55
Buildings - freehold	Up to 60
Fixtures and equipment	Up to 20

The assumed useful economic lives of distribution network assets were changed from 1 April 2007 to those set out above. Prior to 1 April 2007, network assets (other than meters) had a 40 year life. Freehold land is not depreciated.

The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads, but excludes financing costs.

Assets are depreciated on a straight line basis. Customers' contributions towards distribution network assets, which include capital grants, are credited to the profit and loss account. The unamortised amount of such contributions is shown as a deduction from fixed assets. This is a departure from the Companies Act 1985 requirements which require fixed assets to be included at their purchase price or production cost and hence the unamortised amount of contributions would be presented as deferred income. However, contributions relate directly to the cost of fixed assets used in the distribution network and it is the opinion of the directors that the treatment adopted is necessary to give a true and fair view. The value of unamortised contributions is shown in Note 11.

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

1. Accounting policies (continued)

Property

Properties surplus to operational requirements are stated at the lower of cost and net realisable value. Profits are recognised when properties are sold. Sales are accounted for when there is an unconditional exchange of contracts.

Investments

Investment income is included in the Regulatory Financial Statements of the year in respect of which it is receivable. Fixed asset investments are stated at cost less any provisions for impairment. Current asset investments are valued at the lower of cost and net realisable value.

Stocks

Stocks are valued at the lower of cost and net realisable value which takes account of any provision necessary to recognise damage and obsolescence.

Provisions

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

Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Company's taxable profits and its results as stated in the Regulatory Financial Statements that arise from the inclusion of gains and losses in tax assessments in years different from those in which they are recognised in the Regulatory Financial Statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is not recognised when fixed assets are revalued unless by the balance sheet date there is a binding agreement to sell the revalued asset and the gain or loss expected to arise on sale has been recognised in the Regulatory Financial Statements. Neither is deferred tax recognised when fixed assets are sold and it is more likely than not that the taxable gain will be rolled over, being charged to tax only if and when the replacement assets are sold.

Deferred tax is measured at the average tax rates that are expected to apply in the years in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a discounted basis to reflect the time value of money over the period between the balance sheet date and the dates on which it is estimated that the underlying timing differences will reverse. The discount rates used reflect the post-tax yields to maturity that can be obtained on government bonds with similar maturity dates and currencies to those of the deferred tax assets or liabilities.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

2. Segmental reporting

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

3. Operating expenses

The directors consider that the nature of the business is such that the analysis of expenses shown below is more informative than that set out in the formats specified by the Companies Act 1985.

	2008 £m	2007 £m
Cost of sales	**12.1**	14.3
Distribution network expenses	**58.9**	70.8
Other operating expenses	**25.0**	13.0
Operating expenses	**96.0**	98.1

Other operating expenses include certain pension costs, customer service, billing, and administration.

	2008 £m	2007 £m
Operating profit is stated after charging:		
Depreciation	**22.7**	31.5
Loss on sale or disposal of tangible fixed assets	**-**	1.4
Operating lease rentals:		
Plant, machinery and equipment	**0.1**	0.1
Land and buildings	**0.7**	0.7
Research and development	**0.2**	0.1
Auditors' remuneration:		
Fees payable to the Company's auditors for the audit of the Company's annual accounts	**0.2**	0.2
Fees payable for non audit services	**-**	-

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

4. Interest expense (net)

	2008	2007
	£m	£m
Interest payable and similar charges:		
On loans from Group undertakings	**5.6**	0.6
Dividends payable on 7% preference shares	**3.5**	3.5
Other loans	**24.4**	16.8
	33.5	20.9
Interest receivable and similar income:		
On loans to Group undertakings	**(26.7)**	(11.8)
Other	**-**	(0.2)
Interest expense (net)	**6.8**	8.9

5. Other finance income

	2008	2007
	£m	£m
Expected return on pension scheme assets (Note 9(d))	**0.6**	0.6
Interest on pension scheme liabilities (Note 9(d))	**(0.5)**	(0.4)
Other finance income	**0.1**	0.2

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

6. Tax on profit on ordinary activities

(a) Analysis of charge in the year

	2008 £m	2007 £m
Current tax:		
UK corporation tax on profits for the year	**21.3**	21.3
Adjustment in respect of prior years	**(0.8)**	(6.2)
Total current tax (Note 6(b))	**20.5**	15.1
Deferred tax:		
Origination and reversal of timing differences	**0.3**	0.8
Decrease/(increase) in discount	**4.4**	(21.6)
Adjustment in respect of prior years	**0.1**	1.4
Adjustment to pension costs charged	**2.7**	5.3
Reversal of timing differences in respect of industrial buildings	**(1.2)**	-
Impact of change in corporation tax rate	**(9.1)**	-
Total deferred tax (Note 16)	**(2.8)**	(14.1)
Tax charge on profit on ordinary activities	**17.7**	1.0

(b) Factors affecting the current tax charge for the year

The current tax assessed for the year is different to the standard rate of corporation tax in the UK (30%). The differences are explained below:

	2008 £m	2007 £m
Profit on ordinary activities before tax	**82.2**	79.8
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30%	**24.7**	23.9
Effects of:		
Expenses not deductible and income not taxable for tax purposes	**0.1**	(1.6)
Timing difference between capital allowances and depreciation	**(2.0)**	0.9
Other timing differences	**1.7**	(1.7)
Adjustment to tax charge in respect of prior years	**(0.8)**	(6.2)
Adjustment to pension costs charged	**(0.1)**	(0.2)
Group relief surrendered at non-standard rates	**(3.1)**	-
Current tax charge for the year (Note 6(a))	**20.5**	15.1

6. Tax on profit on ordinary activities (continued)

(c) Factor which will effect future tax charges

The standard rate of corporation tax changes to 28% with effect from 1 April 2008.

7. Dividends

	2008 **£m**	2007 £m
Dividends paid on equity shares:		
Interim dividends (1.5 pence per share (2007: 11.9 pence))	**6.0**	48.0

The WPD Group is structured such that debt is held by UK holding companies. Dividends from WPD South Wales and other operating companies fund the interest on this debt.

8. Employee costs and numbers (including executive directors)

(a) Employee costs

	2008 **£m**	2007 £m
Total employee costs during the year amounted to:		
Wages and salaries	**31.3**	30.7
Severance	**0.3**	0.1
Social security costs	**2.6**	2.6
Pension costs - severance related	**0.5**	-
Pension costs - other	**20.1**	8.8
Total employee costs	**54.8**	42.2
Less allocated to capital expenditure	**(24.6)**	(21.3)
Charged to the profit and loss account	**30.2**	20.9

Pension costs exclude those relating to the Western Power Utilities Pension Scheme as a reimbursement agreement is in place (Note 9(e)).

(b) Number of employees
The average number of employees during the year was 878 (2007: 958). The number of staff and costs shown include a proportion of WPD South West staff who work in part for WPD South Wales. The reduction in numbers relates primarily to metering staff who transferred to a third party under the Transfer of Undertaking Protection of Employment Rights Act ("TUPE").

8. Employee costs and numbers (including executive directors) (continued)

(c) Share based payments
The Group issues to directors and senior employees share appreciation rights ("SAR"s) relating to the shares of the WPD Group's ultimate parent, PPL Corporation. The SARs require the Group to pay the intrinsic value of the SAR to the director or employee at the date of exercise. At 31 March 2008, the Group had recorded liabilities of £2.8m (2007: £1.5m). Fair value of the SARs is determined by using the Black-Scholes option-pricing model using the assumptions noted below. In 2008, the Group recorded total expenses of £1.5m (2007: £1.7m) allocated evenly between WPD South West and WPD South Wales. The total intrinsic value at 31 March 2008 was £2.6m (2007: £1.4m).

The inputs into the Black-Scholes option-pricing model were:

	2008	2007
Expected volatility	**20.85%**	21.61%
Expected life (years)	**6**	6
Risk-free rate	**2.95%**	4.85%
Expected dividend yield	**3.10%**	3.31%

Expected volatility was determined by calculating the historical volatility of PPL's share price over the previous 5.4 years. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

9. Pension commitments

(a) Introduction
The Company participates in three defined benefit schemes, the Western Power Distribution Group segment of the Electricity Supply Pension Scheme ("ESPS"), the Infralec 1992 Pension Scheme ("Infralec 92"), and the Western Power Utilities Pension Scheme ("WPUPS").

The ESPS provides pension and other related defined benefits based on final pensionable pay to employees throughout the electricity industry. One segment of the ESPS relates to the WPD Group as a whole and most employees of the Group are members of the ESPS. The assets are held in a trustee administered fund. Under the guidance of FRS 17, where an entity cannot separate out its share of the scheme's assets and liabilities on a reasonable and consistent basis, the relevant entity should account for pensions as if the scheme were a defined contribution scheme, and charge contributions to the profit and loss account and capital expenditure as they become payable in accordance with the rules of the scheme; this has been applied to WPD South Wales. Full FRS 17 disclosure for the ESPS is made in the consolidated financial statements of Western Power Distribution Holdings Limited. A summary is however given below.

The Infralec 92 provides benefits on both a money purchase and final salary basis and is operated by WPD South Wales. The assets are held in a trustee administered fund. As Infralec 92 only relates to past employees of this Company, the pension costs shown in these Regulatory Financial Statements reflect Infralec 92 as a defined benefit scheme and full FRS 17 disclosures are given in this note.

9. Pension commitments (continued)

(a) Introduction (continued)

WPD South Wales is the principal employer for WPUPS, which is a defined benefit scheme providing benefits relating to previous employees of an affiliate group which was previously headed by Hyder plc (now Hyder Limited in liquidation). WPD South Wales will fund the deficit. However, as another WPD Group company (Western Power Distribution Holdings Limited) has taken full financial responsibility for this scheme, WPD South Wales will be reimbursed for these payments. Contributions of £2.9m were paid by the Company and reimbursed during the year ended 31 March 2008 (2007: £8.5m). The value of the reimbursement agreement is stated in the balance sheet (Note 13) and matches the gross liability recorded under FRS 17 (Note 9(e)).

WPD employs a building block approach in determining the rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation at 31 March.

(b) Net liability recognised in the balance sheet

	2008 £m	2007 £m
Infralec 92 (Note 9(d))	**(0.3)**	(1.0)
WPUPS (Note 9(e))	**(10.8)**	(23.0)
Net liability recognised	**(11.1)**	(24.0)

As stated above, WPD South Wales is reimbursed for its liability in respect of WPUPS and the value of this reimbursement agreement is shown in Note 13.

(c) ESPS

As stated above, the ESPS applies across the WPD Group and cannot be reasonably separated between the various Group entities. Under FRS 17, WPD South Wales thus records pension costs for the ESPS on a contributions basis. Full FRS 17 disclosure is given in the accounts of Western Power Distribution Holdings Limited. However, for completeness, a summary is given below.

The financial assumptions used in calculating the figures for ESPS under FRS 17 in respect of the WPD Group were:

	2008	2007
Rate of increase in salaries	**4.55%**	4.05%
Rate of increase to pensions in payment	**3.3%**	2.8%
Discount rate	**6.9%**	5.4%
Inflation	**3.3%**	2.8%

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

9. Pension commitments (continued)

(c) ESPS (continued)

The mortality assumptions are based on the recent actual mortality experience of members within the scheme and the assumptions also allow for future mortality improvements. The assumptions are that a member currently aged 60 will live on average for a further 25.7 years if they are male and for a further 28.1 years if they are female. For a member who retires in 2028 at age 60 the assumptions are that they will live on average for a further 26.9 years after retirement if they are male and for a further 29.2 years after retirement if they are female.

The assets and liabilities of the ESPS for the WPD Group as a whole, at 31 March, were as follows:

	2008 £m	2007 £m
Present value of obligations	**1,251.9**	1,387.3
Fair value of plan assets	**(1,180.1)**	(1,264.1)
Deficit in the scheme	**71.8**	123.2
Related deferred tax asset	**(20.1)**	(37.0)
Net pension liability	**51.7**	86.2

Employer contributions paid to the ESPS in respect of the WPD Group were £39.3m (2007: £38.9m). Contributions in 2007 included a prepayment of £14.9m made in respect of contributions due in 2008. ESPS pension costs born by WPD South Wales are the full amounts as shown in Note 8. Employer contributions expected to be paid to the ESPS during the year ending 31 March 2009 amount to £53.1m.

(d) Infralec 92

The financial assumptions used in calculating the figures for Infralec 92 under FRS 17 were:

	2008	2007
Rate of increase to pensions in payment	**3.3%**	2.8%
Discount rate	**6.9%**	5.4%
Inflation	**3.3%**	2.8%

The mortality assumptions are based on the recent actual mortality experience of members of the ESPS scheme (as the Infralec 92 scheme is not large enough for a credible mortality analysis to be carried out). The assumptions also allow for future mortality improvements. The assumptions are that a member currently aged 60 will live on average for a further 25.7 years if they are male and for a further 28.1 years if they are female. For a member who retires in 2028 at age 60 the assumptions are that they will live on average for a further 26.9 years after retirement if they are male and for a further 29.2 years after retirement if they are female.

9. Pension commitments (continued)

(d) Infralec 92 (continued)

The amounts recognised in the balance sheet are as follows:

	2008 £m	2007 £m
Present value of obligations	**8.0**	9.2
Fair value of plan assets	**(7.6)**	(7.7)
Deficit in the scheme	**0.4**	1.5
Related deferred tax asset	**(0.1)**	(0.5)
Net pension liability	**0.3**	1.0

The expected rate of return for major categories of plan assets at the balance sheet date are as follows:

	2008 %	2007 %
Equities	**9.0**	9.0
Corporate bonds	**6.9**	5.4
Gilts	**4.5**	4.7
Cash and other	**6.0**	5.5
Average expected long-term rate of return	**7.8**	7.9

The major categories of plan assets as a percentage of total plan assets are as follows:

	2008 %	2007 %
Equities	**70**	73
Corporate bonds	**2**	1
Gilts	**23**	21
Cash and other	**5**	5

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

9. Pension commitments (continued)

(d) Infralec 92 (continued)

Analysis of profit and loss charge:

	2008 £m	2007 £m
Expected return on scheme assets	**0.6**	0.6
Interest on scheme liabilities	**(0.5)**	(0.4)
Credit recognised in profit and loss account	**0.1**	0.2

Changes to the present value of the defined benefit obligation are as follows:

	2008 £m	2007 £m
Defined benefit obligation at 1 April	**9.2**	8.9
Interest cost	**0.5**	0.4
Actuarial (gains)/losses on scheme liabilities	**(1.4)**	0.4
Net benefits paid out	**(0.3)**	(0.5)
Defined benefit obligation at 31 March	**8.0**	9.2

Changes to the fair value of the scheme assets are as follows:

	2008 £m	2007 £m
Fair value of scheme assets at 1 April	**7.7**	7.4
Expected return on scheme assets	**0.6**	0.6
Actuarial losses on scheme assets	**(0.7)**	(0.2)
Employer contributions	**0.3**	0.4
Net benefits paid out	**(0.3)**	(0.5)
Fair value of scheme assets at 31 March	**7.6**	7.7

9. Pension commitments (continued)

(d) Infralec 92 (continued)
Actual return on scheme assets:

	2008 £m	2007 £m
Expected return on scheme assets	**0.6**	0.6
Actuarial losses on scheme assets	**(0.7)**	(0.2)
Actual return on scheme assets	**(0.1)**	0.4

Cumulative actuarial gains and losses recognised in equity:

	2008 £m	2007 £m
Cumulative actuarial gains at 1 April	**0.4**	1.0
Net actuarial gains/(losses) recognised in the year	**0.7**	(0.6)
Cumulative actuarial gains at 31 March	**1.1**	0.4

History of present value of liabilities, asset values, deficit in scheme and experience gains and losses:

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Present value of defined benefit obligations	**8.0**	9.2	8.9	8.4	8.0
Fair value of scheme assets	**(7.6)**	(7.7)	(7.4)	(5.9)	(5.2)
Deficit in the scheme	**0.4**	1.5	1.5	2.5	2.8
Experience gains and (losses) on scheme liabilities * :					
Amount (£m)	**0.1**	(0.3)	-	0.1	(0.8)
Experience gains and (losses) on scheme assets:					
Amount (£m)	**(0.7)**	(0.2)	0.9	0.3	0.5

* Does not include the effect of changes to actuarial assumptions.

The contributions expected to be paid to the scheme during the financial year ended 31 March 2009 amount to £0.3m.

9. Pension commitments (continued)

(e) WPUPS

WPD South Wales is the principal employer for WPUPS, which is a defined benefit scheme providing benefits to previous employees of an affiliate group and was transferred to WPD South Wales in April 2002. The assets of the scheme are held separately from those of the Company in trustee administered funds. However, another WPD Group company (Western Power Distribution Holdings Limited) has taken full financial responsibility for this scheme and reimburses WPD South Wales for contributions it pays to WPUPS. The value of the reimbursement agreement is stated in the balance sheet (Note 13) and matches the deficit in the scheme recorded under FRS 17 as shown below.

The principal actuarial assumptions at the balance sheet date are set out below:

	2008	2007
Inflation	**3.3%**	2.8%
Rate of increase to pensions in payment	**3.3%**	2.8%
Discount rate for scheme liabilities	**6.9%**	5.4%

The mortality assumptions are based on the recent mortality experience of members within the scheme and the assumptions also allow for future mortality improvements. The assumptions are that a member currently aged 60 will live on average for a further 24.6 years if they are male and for a further 27.1 years if they are female. For a member who retires in 2028 at age 60 the assumptions are that they will live on average for a further 26.0 years after retirement if they are male and for a further 28.3 years after retirement if they are female.

In order to eliminate the funding deficit, the Company is paying contributions of £6.0m per annum from 1 April 2008 for 8 years, payable quarterly in arrears and increasing in line with the Retail Prices Index on an annual basis. This will be subject to change at the next formal actuarial review.

The amounts recognised in the balance sheet are as follows:

	2008 £m	2007 £m
Present value of obligations	**327.6**	365.2
Fair value of plan assets	**(312.6)**	(332.4)
Deficit in the scheme	**15.0**	32.8
Related deferred tax asset	**(4.2)**	(9.8)
Net pension liability	**10.8**	23.0

9. Pension commitments (continued)

(e) WPUPS (continued)

The expected rate of return for major categories of plan assets at the balance sheet date are as follows:

	2008	2007
	%	%
Equities	**9.0**	9.0
Government bonds	**4.5**	4.7
Other	**6.0**	5.5
Average expected long-term rate of return	**7.3**	7.9

The major categories of plan assets as a percentage of total plan assets are as follows:

	2008	2007
	%	%
Equities	**62**	73
Government bonds	**35**	22
Other	**3**	5

Analysis of profit and loss charge:

	2008	2007
	£m	£m
Expected return on scheme assets	**25.3**	25.6
Interest on scheme liabilities	**(19.3)**	(17.2)
Movement in reimbursement agreement recognised	**(6.0)**	(8.4)
Total recognised in profit and loss account	**-**	-

Changes to the present value of the defined benefit obligation are as follows:

	2008	2007
	£m	£m
Defined benefit obligation at 1 April	**365.2**	361.5
Interest cost	**19.3**	17.2
Net benefits paid out	**(17.3)**	(17.4)
Settlements	**-**	(1.8)
Actuarial (gains)/losses on scheme liabilities	**(39.6)**	5.7
Defined benefit obligation at 31 March	**327.6**	365.2

9. Pension commitments (continued)

(e) WPUPS (continued)

Changes to the fair value of scheme assets are as follows:

	2008	2007
	£m	£m
Fair value of scheme assets at 1 April	**332.4**	326.5
Expected return on assets	**25.3**	25.6
Contributions - employer	**2.9**	8.5
Net benefits paid out	**(17.3)**	(17.4)
Settlements	**-**	(1.8)
Actuarial losses on scheme assets	**(30.7)**	(9.0)
Fair value of scheme assets at 31 March	**312.6**	332.4

Actual returns on scheme assets are:

	2008	2007
	£m	£m
Expected return on scheme assets	**25.3**	25.6
Actuarial losses on scheme assets	**(30.7)**	(9.0)
Actual return on scheme assets	**(5.4)**	16.6

Cumulative actuarial gains and losses recognised in equity:

	2008	2007
	£m	£m
Cumulative actuarial gains at 1 April	**4.5**	19.2
Net actuarial gains/(losses) recognised in the year	**8.9**	(14.7)
Cumulative actuarial gains at 31 March	**13.4**	4.5

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

9. Pension commitments (continued)

(e) WPUPS (continued)

History of present value of liabilities, asset values, deficit in scheme and experience gains and losses:

	2008	2007	2006	2005	2004
	£m	£m	£m	£m	£m
Present value of defined benefit obligations	**327.6**	365.2	361.5	351.9	317.3
Fair value of scheme assets	**(312.6)**	(332.4)	(326.5)	(270.9)	(253.8)
Deficit in the scheme	**15.0**	32.8	35.0	81.0	63.5
Experience (losses)/gains on scheme liabilities * :					
Amount (£m)	**(5.8)**	4.1	-	(14.3)	11.0
Experience (losses)/gains on scheme assets:					
Amount (£m)	**(30.7)**	(9.0)	47.2	11.6	29.6

* Does not include the effect of changes in assumptions.

The contributions expected to be paid to the scheme during the financial year ended 31 March 2009 amount to £6.0m. These will be reimbursed under a reimbursement agreement with another Group company.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

10. Directors' emoluments

The service contracts for the executive directors are with WPD South West. However, their emoluments include those for services to the WPD Group as a whole, which principally comprises WPD South West and WPD South Wales. The emoluments detail given in this note represents total emoluments of the directors for all services provided to WPD Group companies. The costs are born evenly by WPD South Wales and WPD South West.

	Highest paid director		**Total**	
	2008	2007	**2008**	2007
	£000	£000	**£000**	£000
The combined emoluments of the executive directors comprised:				
Base salary (note i)	**350**	325	**774**	724
Performance dependent bonus (note ii)	**311**	284	**619**	570
Long term incentive plan (note iii)	**385**	579	**385**	1,052
Pension compensation allowance (note iv)	**200**	182	**528**	487
Fees to the independent non executive director (note vi)	**-**	-	**15**	15
	1,246	1,370	**2,321**	2,848

(i) Base salary also includes benefits in kind.

(ii) The amount of the annual bonus is based on the WPD Group's financial performance, improvements in the reliability of the electricity network, customer satisfaction, and other factors.

(iii) Under a long term incentive plan, the three executive directors receive phantom stock options. The option price is set at the quoted share price of the WPD Group's parent in the US, PPL Corporation, at the date the phantom options are granted. The options may be exercised during fixed periods and the gain is payable through the payroll. The values above include any payments made to the executive directors in respect of gains in value of phantom options exercised in the year. In 2008, no executive directors exercised options (2007: three). In addition, WPD's Chief Executive Officer is also a Vice President of PPL Global. As a result, he also receives annually a grant of PPL Corporation shares which he cannot generally access for 3 years. The value of these shares is shown within this line.

(iv) In anticipation of the change in tax applicable to UK pensions effective 6 April 2006, the executive directors resigned as active members of the Electricity Supply Pension Scheme ("ESPS" - Note 9) on 5 April 2006 and elected for enhanced protection. WPD thus no longer contributes for ongoing service to the ESPS in respect of the executive directors. Instead, WPD pays cash compensation to them individually equivalent to the value of WPD's contribution into the ESPS that would have been made had they remained active members (as determined by external actuaries).

(v) The three executive directors are deferred members of the ESPS (see (iv) above). At 31 March 2008, the highest paid director had accrued annual pension benefits of £326,737 (2007: £299,019). The benefits shown assume that an option to convert an element of the annual benefits to a lump sum payable on retirement is not exercised.

(vi) The Group's independent UK non executive director is entitled to fees as determined by the Western Power Distribution Holdings Limited Board. No emoluments are paid to US based non executive directors, who are officers of PPL, in respect of their services as directors to the WPD Group.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

11. Tangible fixed assets

	Leasehold improvements	Distribution network	Fixtures & equipment	Deduct: customers' contributions	Total
	£m	£m	£m	£m	£m
Cost					
At 1 April 2007	0.2	1,334.2	35.2	(266.7)	1,102.9
Additions	-	87.3	5.3	(25.9)	66.7
Disposals	-	(13.6)	(20.9)	-	(34.5)
At 31 March 2008	0.2	1,407.9	19.6	(292.6)	1,135.1
Depreciation					
At 1 April 2007	-	460.9	25.7	(97.3)	389.3
Charge for the year	-	24.8	3.7	(4.0)	24.5
Disposals	-	(13.6)	(20.8)	-	(34.4)
At 31 March 2008	-	472.1	8.6	(101.3)	379.4
Net book value					
At 31 March 2008	**0.2**	**935.8**	**11.0**	**(191.3)**	**755.7**
At 1 April 2007	0.2	873.3	9.5	(169.4)	713.6

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

	2008	2007
	£m	£m
Freehold	**38.8**	33.7
Short leasehold	**0.2**	0.2

Included within the Company's fixed assets are assets in the course of construction amounting at 31 March 2008 to £6.7m (2007: £4.8m) and land at a cost of £11.9m (2007: £10.4m).

Leasehold improvements above relate to a non-network property held on a long term lease. Customers' contributions relate entirely to the construction of the network.

During the year the Company reviewed the useful economic lives of its distribution network assets. Effective 1 April 2007, after considering information from Ofgem and other internal and external surveys, the weighted average useful lives of network assets (excluding meters) were extended from 40 years to an average of approximately 54 years. The effect of this revision is a reduction in the charge to profit before tax for the year of £12.9m.

12. Stocks

	2008 £m	2007 £m
Raw materials and consumables	**0.7**	0.6
Work in progress	**0.2**	1.3
	0.9	1.9

13. Debtors

	2008 £m	2007 £m
Amounts falling due within one year:		
Trade debtors	**31.0**	29.2
Amounts owed by Group undertakings	**365.4**	365.1
Other debtors	**0.3**	0.5
Prepayments	**1.1**	6.8
Reimbursement agreement re WPUPS (note 9(e))	**6.0**	2.8
	403.8	404.4
Amounts falling due after one year:		
Reimbursement agreement re WPUPS (note 9(e))	**9.0**	30.0

Amounts owed by Group undertakings are unsecured and are repayable on demand.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

14. Creditors

	2008	2007
	£m	£m
Amounts falling due within one year:		
Trade creditors	**2.7**	3.2
Amounts owed to Group undertakings	**65.6**	101.4
UK corporation tax	**38.7**	18.2
Other creditors	**18.6**	18.0
Accruals and deferred income	**15.7**	18.1
	141.3	158.9
Amounts falling due after more than one year:		
Unsecured borrowings repayable after more than five years:		
£150m 9.25% Eurobonds 2020	**148.7**	148.6
£225m 4.804% bonds 2037	**218.2**	218.0
50,000,000 preference shares (7% net) of £1 each	**50.0**	50.0
	416.9	416.6

Amounts owed to Group undertakings are unsecured and are repayable on demand.

Unsecured borrowings are stated net of unamortised issue costs of £8.1m (2007: £8.4m). These costs together with the interest expense are allocated to the profit and loss account over the term of the bonds at a constant rate on the carrying amount.

Preference shares

The number of shares authorised and allotted at both 31 March 2008 and 2007 was 50,000,000 at £1 each. They are held by another WPD Group company and carry a fixed dividend. Dividends are payable every six months, in arrears, on 31 March and 30 September. Payment can be delayed but any dividends outstanding must be settled before dividends on ordinary shares can be paid. The shares have no redemption entitlement. On a winding up, the holders have priority before all other classes of shares to receive repayment of capital plus any arrears of dividend. The holders have no voting rights unless the dividend is in arrears.

15. Provisions for liabilities and charges

	Deferred taxation (Note 16)	Other	Total
	£m	£m	£m
At 1 April 2007	67.0	0.9	67.9
Released during the year	(5.6)	-	(5.6)
At 31 March 2008	**61.4**	**0.9**	**62.3**

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

15. Provisions for liabilities and charges (continued)

Other provisions at 31 March 2008 relate to an expected settlement of a liability to the Electricity Association Limited and Electricity Association Technology Limited primarily relating to a pension deficit in those companies. These liabilities are being settled over a period of approximately 6 and 9 years, respectively.

16. Deferred tax

	2008 £m	2007 £m
Accelerated capital allowances	**122.1**	130.0
Other timing differences	**2.7**	4.8
Undiscounted provision for deferred tax	**124.8**	134.8
Discount	**(63.4)**	(67.8)
Discounted provision for deferred tax (Note 15)	**61.4**	67.0
Deferred tax asset on pension liability (Note 9)	**(4.3)**	(10.3)
Provision at end of year including deferred tax on pension liability	**57.1**	56.7

	2008 £m	2007 £m
Provision for deferred tax at 1 April	**56.7**	74.2
Deferred tax credit in profit and loss account (Note 6(a))	**(2.8)**	(14.1)
Charged/(credited) to statement of total recognised gains and losses	**3.2**	(3.4)
Provision for deferred tax at 31 March	**57.1**	56.7

17. Called-up share capital

	2008 £	2007 £
Authorised:		
405,000,000 ordinary shares of 50p each	**202,500,000**	202,500,000
One special rights redeemable preference share of £1	**1**	1
Allotted, called-up and fully paid:		
403,442,224 ordinary shares of 50p each	**201,721,112**	201,721,112

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

18. Reconciliation of movements in shareholders' funds

	2008 £m	2007 £m
Profit for the financial year	**64.5**	78.8
Dividends on equity shares	**(6.0)**	(48.0)
Net movement in hedging reserve	**(0.2)**	3.1
Other recognised losses and gains relating to the year	**(3.0)**	4.0
Net increase in shareholders' funds	**55.3**	37.9
Opening shareholders' funds	**482.5**	444.6
Closing shareholders' funds	**537.8**	482.5

19. Reserves

	Share premium account £m	Capital redemption reserve £m	Hedging reserve £m	Profit & loss account £m
At 1 April 2007	23.2	5.1	9.5	243.0
Actuarial gain recognised in pension schemes (Note 9)	-	-	-	9.6
Movement on deferred tax relating to actuarial gain recognised above	-	-	-	(2.9)
Impact of tax rate change on cumulative actuarial gains	-	-	-	(0.8)
Reimbursement agreement relating to WPUPS pension scheme (Note 9(e))	-	-	-	(8.9)
Cash flow hedges transfer to net profit (net of tax)	-	-	(0.2)	-
Profit for the financial year	-	-	-	64.5
Dividends on equity shares	-	-	-	(6.0)
At 31 March 2008	**23.2**	**5.1**	**9.3**	**298.5**

The share premium account arose on the issue of shares under share option schemes and the capital redemption reserve is in respect of the purchase of its own shares by the Company, both prior to 1996.

The hedging reserve relates to value received in respect of interest rate derivatives entered into in anticipation of the issue of long-term debt. The gain is being amortised through the profit and loss account over the term of the debt.

6.7 Notes to the Regulatory Financial Statements

For the year ended 31 March 2008

20. Capital and other commitments

a) There are annual commitments under operating leases which expire :

	2008 **£m**	2007 £m
Over five years - land and buildings	**0.1**	0.1

b) Fixed asset expenditure contracted but not provided in the Regulatory Financial Statements at 31 March 2008 was £1.1m (2007: £3.1m).

21. Related party transactions

The Company, a wholly-owned subsidiary undertaking, has taken the exemption available from related party disclosure requirements of FRS 8 as the financial statements of a parent company are available to the public (Note 22).

22. Ultimate parent undertaking

The immediate parent undertaking of the Company is Western Power Distribution LLP, which is registered in England and Wales.

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

The largest group in which the results of the Company are consolidated is that headed by PPL Corporation, which is the ultimate parent undertaking. Copies of their accounts may be obtained from Two North Ninth Street, Allentown, Pennsylvania, PA18101-1179, US.

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