Scottish Hydro-Electric Power Distribution Limited

Regulatory Accounts for the year ended 31 March 2006

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Scottish Hydro-Electric Power Distribution Limited

Corporate Report for the year ended 31 March 2006

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Scottish Hydro-Electric Power Distribution Limited

Corporate Report: Review of the Year to 31 March 2006

Scottish Hydro-Electric Power Distribution Limited (the Company) is a wholly owned subsidiary of Scottish and Southern Energy plc (the Group). The Company's first responsibility is to maintain safe and reliable supplies of electricity and to restore supplies as quickly as possible in the event of interruptions. In line with this it is encouraging that our performance across a range of measures continues to be good. This performance has been achieved while maintaining close control over the operating cost base and confirms that the electricity networks managed by the Group are among the most efficient in the world.

The Company is the subject of incentive-based regulation by the Office of Gas and Electricity Markets (Ofgem), which sets for periods of five years the prices that can be charged for the use of the electricity network, the capital expenditure and the allowed operating expenditure. In broad terms, Ofgem seeks to strike the right balance between attracting investment in electricity, encouraging companies to operate the networks as efficiently as possible and ensuring that prices for customers are no higher than they need to be. As at 31 March 2006, the Group estimates that Ofgem's valuation of the assets of the Company's distribution business (the Regulated Asset Value or 'RAV') was approximately £780m.

Operating profit for the Company increased by 1.6% to £103.1m. This reflected an increase in the number of units distributed and follows the introduction of the new Price Control for 2005-10 and improved performance under Ofgem's incentives framework. In the Scottish Hydro-Electric area, 8.9TWh of electricity were distributed during 2005/06, compared with 8.7TWh in the previous year.

The average number of minutes of lost electricity supply per customer was 65, compared with 86 in the previous year, making performance in 2005/06 the best since records began in the 1960s. The number of interruptions per 100 customers was 79, compared with 89 in the previous year. Performance in respect of both minutes lost and interruptions was ahead of Ofgem's Quality of Supply incentive targets. This together with income earned under other incentive arrangements is expected to lead to additional revenue of over £4m in 2007/08.

Electricity Network Investment

The key responsibility of the Company's businesses is to maintain safe and reliable supplies of electricity and to restore supplies as quickly as possible in the event of interruptions. During the Price Control period 2000-05, the Company invested £204.8m in its electricity network. A further £42.9m was invested in 2005/06. In the course of the year, the Company added 270km to the length of its networks, taking the total to over 45,000km. It also rebuilt 2,520km of its networks as part of its programme of replacing 'open wire' overhead lines.

The Price Control Review for 2005-10 resulted in increased allowances for capital expenditure to maintain and improve the electricity networks, and the Company's increased investment programme is now under way.

As a result, the estimated RAV of the Company's distribution business has increased by approximately £10m (nominal) to around £780m as at 31 March 2006. In addition, the Company expects to increase capital expenditure to approximately £55M in 2006/07 and to sustain capital expenditure at this level until 2010. On this basis, the RAV is expected to grow by around £50m in nominal terms during the 2005-2010 Price Control period.

Electricity Distribution Priorities in 2006/07

During 2006/07, the Company's first objective will be to maintain safe and reliable supplies of electricity and to restore supplies as quickly as possible in the event of interruptions. This will be supported by an increase in investment in the network, targeted at upgrading them where the greatest number of customers will benefit.

Scottish Hydro-Electric Power Distribution Ltd

Corporate Report: Review of the Year to 31 March 2006

1 Operational Review

1.1 Factors affecting the Business

The Company is responsible for managing an electricity distribution network, serving more than 700,000 customers. Distribution of electricity within specified areas is a monopoly activity and the income earned by charging electricity customers for the use of the wires is closely regulated by Ofgem, as is the level of investment which is made in electricity networks. The Company has completed the first year of the price controls set for the period up to 31 March 2010.

Against this background, the Company's objective is to manage the consequences of the growth in demand for electricity and ensure the network has the minimum number of faults and the maximum robustness in the face of severe weather and other supply interruption risks. It is also important to automate networks so that when supply is interrupted, it can be restored as soon as possible. The programme of investment is designed with these goals in mind.

1.2 Use of Resources and Status of Significant Projects

In line with the policies in place to achieve the objectives highlighted at 1.1, a total of £42.9m was invested in the electricity network. Investment of this kind upgrades the electricity network and reinforces the value of the RAV which, in turn, supports the ongoing value of the business.

In the Scottish Hydro-Electric Power Distribution area, the programme to upgrade and refurbish the network continued during 2005/06, with 2,260km of high voltage overhead lines and 260km of low voltage lines refurbished.

The programme of network automation continued, with another 283 new radio-controlled automated switching units in rural areas, allowing for faster restoration of supply to customers.

In 2005/06, the Company distributed 8.9TWh of electricity, an increase of 0.15TWh. The average number of minutes of lost electricity supply per customer was 65, which was within the Quality of Supply incentive targets set by Ofgem for the 2005-10 Price Control Period, which gives financial benefits to distribution network operators that deliver good performance for customers. The number of supply interruptions per 100 customers was 79.

The Company was a 'benchmark' company and was not given any company-specific actions by the DTI commissioned report into power systems emergencies published at the end of 2002. Nevertheless, it has implemented a number of initiatives to improve further the resilience of the electricity network for the future. For example, falling trees or clashing branches are a major source of supply interruptions during windy weather conditions. To improve performance in this area, the Group has started employing directly most of the people involved in tree cutting. This is also in line with the Group's general approach that operations and services are best managed and delivered by people who are directly employed by the company.

Scottish Hydro-Electric Power Distribution Ltd

Corporate Report: Review of the Year to 31 March 2006

1 Operational Review (continued)

1.3 Employees

Enabling employees to derive the maximum possible benefit from their employment with the Group is one of the principles which has been adopted. The Board believes that this can be achieved through active encouragement of share ownership, participation in the Group's affairs, and the maintenance of effective policies on issues such as equal opportunities.

Participation in the Group's affairs is encouraged through team meetings, briefing documents and an internal magazine. During the year, employees were invited to attend business development and financial results briefings. Policies on such matters as Equal Opportunities and Health and Safety are regularly communicated to staff.

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

1.4 Safety

The Group believes that all work can be done in such a way that no-one, whether an employee, contractor, customer or member of the community, suffers from its operations. It believes that all injuries are preventable and it aims to provide staff with training, work methods and equipment to achieve that goal.

'Being safe' is a core value in the business. In line with this, the Group's Health, Safety and Environment Manual, which has the status of a work instruction, emphasises that safety will not be compromised for business interest or operational pressures and all injuries, plant damage and near misses will be reported and investigated. The Director with lead responsibility for Health and Safety is Colin Hood.

The net result of this commitment to safety is that Scottish and Southern Energy plc continues to lead Britain's electricity industry in safety.

1.5 Principal risks and uncertainties

As the Company operates a regulated monopoly electricity network under a licence issued by Ofgem, one of the major risks arises from the quinquennial price review when the future income that the business may collect from the users of the electricity network is set. The current price control period runs from 1 April 2005 to 31 March 2010 and discussions on the next price control will start in 2008. In arriving at the allowed income Ofgem assess the revenue and capital expenditure plans of the business and determine an efficient level of that expenditure. In addition, they assess the quality of service requirements for the network and determine a cost of capital sufficient to encourage the required investment in the network. Given the importance of the outcome of the price control review process, the establishment of allowable income for the following five years, the Company invests considerable management time to ensure that the correct price control is set.

In the short term, the electricity network can be subject to damage, and potentially major disruption, by the weather. Storms caused by winter weather fronts, winter snow fall and lightning storms at any time of year can damage the electricity distribution network and result in customers' supply of electricity being interrupted. To mitigate the effects of these events, weather forecasts are closely monitored and staff deployed in advance of foreseeable major weather events. Arrangements are in place to use resources from contractors and other electricity distribution network operators in the event of major interruptions and contracts are in place with suppliers of materials and services which can be brought into action at short notice in the event of severe weather.

Scottish Hydro-Electric Power Distribution Ltd

Corporate Report: Review of the Year to 31 March 2006

2. Financial Review

2.1 Balance Sheet

The Group and Company both continue to maintain one of the strongest balance sheets in the global utility sector, and both hold an *A+/Aa3* long-term credit rating. This gives the Company significant competitive advantage in terms of cost of funding and supporting new developments.

The Group adopted IAS 19 in full for the treatment of pension scheme assets, liabilities and costs. The majority of employees of the Company are members of the Scottish Hydro-Electric Pension Scheme, which, at 31 March 2006, had an IAS 19 surplus, net of deferred tax, of £63.1M (2005 - £69.2M).

2.2 Financial Risk Management

The Company's financial risk is managed as part of the wider group risk management policy.

The Company's operations are financed by a combination of retained profits, bank borrowings, long term debt issuance and inter company loan stocks.

The main financial risks affecting the Group include exposures to fluctuations or changes in interest rates, foreign exchange rates, liquidity, commodity prices and volumes and counterparty creditworthiness. The Group's Risk Committee, which reports to the Board, reviews and agrees policies for addressing each of these risks. At 31 March 2006, 83.2% of the Group's borrowings were at fixed rates, after taking account of interest rate swaps. The Company's main risk area is in relation to interest rates and, as noted, this is managed as part of the Group's risk policies.

2.3 Taxation

The Company's effective current tax rate was 35.2% compared with 29.5% in the previous year, after prior year adjustments. The headline effective tax rate is 34.4% compared with 31.9% in the previous year.

2.4 Dividend

The Company's dividend policy was to distribute up to 50% of surplus cash flow as a dividend for both years.

2.5 Accounting policy for connections and capital contributions.

The Company provides financial support to individuals wishing to connect to its distribution network. This support, known as the DUoS allowance, is available whether or not the Company carries out the actual connection works. The cost of the support is capitalised by the Company and depreciated over 40 years.

Scottish Hydro-Electric Power Distribution Ltd

Corporate Report: Review of the Year to 31 March 2006

2. Financial Review (continued)

2.6 Borrowings and Facilities

The Company has loans of £375.0m (2005 – £475.0m) of which £300m (2005 - £400m) is due to other group companies and £75.0m (2005 - £75.0m) is in the form of loans from the European investment Bank. Of the total, interest is paid at fixed rates on £350.0m (2005 - £350.0m).

As at 31 March 2006, the weighted average interest rate payable was 5.86% (2005 – 5.75%) and the weighted average remaining term was 14.22 years (2005 – 12.22 years).

2.7 International Financial Reporting Standards

The application of International Financial Reporting Standards (IFRS) is required for listed companies for accounting periods commencing on or after 1 January 2005. As a result, the Group's financial statements for the year to 31 March 2006 have been prepared in accordance with EU adopted IFRS.

The accounts of Scottish Hydro-Electric Power Distribution Limited have been prepared in accordance with applicable UK Generally Accepted Accounting Principles (UK GAAP). A number of the Company's accounting policies have been changed in the accounts to 31 March 2006 following the adoption of a number of new accounting standards issued by the Accounting Standards Board (ASB) as part of the project to converge UK GAAP with adopted IFRS. A fuller explanation of the changes in the Company's accounting policies is included in the Notes to the Accounts, Notes 1 and 2.

Scottish Hydro-Electric Power Distribution Limited

Corporate Governance Statement

Scottish and Southern Energy plc Group ("The Group")

The Board continues to commit to the highest standards of corporate governance, and has due regard to the continuing developments in this field. The Group seeks to run its entire business and maximise profits in a way which is responsible, safe, customer focused and commercially aware. These are the four core values which underlie everything the Group does. Moreover, the Group aims to conduct its business in an ethical manner that maintains an appropriate balance between social, economic and environmental issues.

In keeping with this, the Group has continued its commitment to high standards of corporate governance.

Throughout the year the Group has complied with the provisions of the Combined Code except for the following matter. As explained last year, Henry Casley retired as a non-Executive Director on 17 May 2005. He was considered not to be independent in terms of the Combined Code. Since 17 May 2005, the Group has complied with all the provisions set out in section 1 of the Combined Code. Taking account of the above explanation, the Board therefore considers that the Group has satisfied its obligations under the Combined Code.

The composition of the Board comprises a non-Executive Chairman, four Executive Directors and four independent non-Executive Directors, which complies with the Combined Code provisions in this regard.

The Board acknowledges its responsibility for ensuring that an adequate system of internal control exists which accords with the requirements of the Turnbull Committee guidance.

Scottish Hydro-Electric Power Distribution Limited ("The Company")

Board of Directors

The Board consists of three Directors, two of whom are Directors of the Group. None of the Directors are Directors of Group Companies involved in Supply or Generation activities. The Group has an Audit Committee, a Remuneration Committee, an Executive Committee, a Risk Committee, a Health, Safety and Environmental Advisory Committee and a Nomination Committee and details of the appointees are included in the published Corporate Governance Statement of the Group. The Company, as a subsidiary entity, has no such Committees.

Internal Control

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

No system of control can, however, provide absolute assurance against material mis-statement or loss. Accordingly, the Directors have regard to what controls, in their judgement, are appropriate to the Company's business, to the materiality of the risks inherent in the business, and to the relative costs and benefits of implementing specific controls. The Board maintains an ongoing process of identifying, evaluating and managing the key commercial, financial and general risks to the Company's business. This process is regularly reviewed by the Board and has been in place for the whole year.

Scottish Hydro-Electric Power Distribution Ltd

Corporate Governance Statement

Scottish Hydro-Electric Power Distribution Limited ("The Company") (continued)

Control is maintained through an organisational structure with clearly defined responsibilities, authority levels and lines of reporting; the appointment of suitably qualified staff in specialised business areas; and continuing investment in high quality information systems. These methods of control are subject to periodical review as to their implementation and continued suitability, and have been in place throughout the year and up to the date of approval of the accounts.

There are established procedures in place for regular budgeting and reporting of financial information. The Company's performance is reviewed by the Directors. Reports include variance analysis and projected forecasts for the year compared to approved budgets and non-financial performance indicators.

There are policies in place covering a wide range of issues such as financial authorisations, IT procedures, health and safety and environmental risks. The business risks associated with the Company's operations are regularly assessed by the Directors.

The effectiveness of the systems of internal control is monitored by the internal audit department. Their reports, which include where appropriate relevant action plans, are distributed to senior managers and Directors.

Environment

The Group manages a wide range of environmental issues. Operating the power systems network is recognised as a priority area and formal environmental management systems have been developed across the Group. The systems have five main elements, based on the established management cycle of (1) setting policy, (2) planning, (3) implementing and operating, (4) checking and correcting and (5) reviewing.

The system exists to enable managers to deliver the Group's environmental policies through procedures and work instructions. It reflects an integrated, Group-wide health and safety and environmental management system.

Going Concern

The Directors consider that the Company has adequate resources to continue in operational existence for the foreseeable future. The accounts are therefore prepared on a going concern basis.

Scottish Hydro-Electric Power Distribution Limited

Report of the Directors

The Report of the Directors of the Company is included in the Regulatory Financial Statements section of these Accounts as part of the Audited Statutory Accounts.

Scottish Hydro-Electric Power Distribution Limited

Statement of Directors' Responsibilities in Respect of the Regulatory accounts and Compliance with Standard Licence Condition 42

The licensee is required by standard condition 42 of the Electricity Distribution Licence to deliver to the Authority regulatory accounts prepared for each financial year ending on 31 March.

Scottish Hydro-Electric Power Distribution Limited

Regulatory Financial Statements for the year ended 31 March 2006

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Scottish Hydro-Electric Power Distribution Limited

Report of the Directors

The Directors present their report together with the audited Accounts for the year ended 31 March 2006.

1. Principal Activities

The Company's principal activity during the year was the regulated distribution of electricity.

2. Business Review

The Company is responsible for managing an electricity distribution network, serving more than 700,000 customers in the North of Scotland. Distribution of electricity within specified areas is a monopoly activity and is closely regulated by the Office of Gas and Electricity Markets (Ofgem), as is the level of investment which is made in electricity networks.

Review of development and performance of the Company

The year to 31 March 2006 was the first year of the current distribution price control period and this along with an increase in units distributed in the year has resulted in increased revenue and profitability for the company. Operating Profit increased by 1.6% to £103.1M.

At the same time the level of investment in the network has also increased in the year in order that the network can be maintained and improved. In 2005/06 the capital expenditure was £42.9M and this level of investment is expected to increase in 2006/07 and in the remaining years of the current price control period. In 2005/06 a further 270km in length was added to the network and 2,520km were rebuilt.

The operational performance of the company continued to improve with a reduction in the number of customer minutes lost to 65 per customer and the number of supply interruptions per 100 customers falling to 79. This is an improvement on the performance in 2004/05 and the company's best performance in these areas since records began in the 1960's. This, along with other incentives established in the price control agreement, is expected to contribute towards additional income of approximately £4M in 2007/08.

Principal Risks and Uncertainties

As noted, the Company is responsible for managing a regulated electricity distribution network, based in the North of Scotland. One of the major risks arises from the quinquennial price review when the future income that the company may collect from the users of the electricity network is set. The current price control period runs from 1 April 2005 to 31 March 2010 and discussions on the next price control will start in 2008. The year to 31 March 2006 is the first year of the current price review period. In arriving at the allowed income Ofgem assess the revenue and capital expenditure plans of the business and determine an efficient level of that expenditure. In addition they assess the quality of service requirements for the network and determine a cost of capital sufficient to encourage the required investment in the network. Given the importance of the outcome of the price control review process, the establishment of allowable income for the following five years, the Company invests considerable management time to ensure that the correct price control is set.

The key responsibility of the Company is to maintain safe and reliable supplies of electricity and to restore supplies as quickly as possible in the event of interruptions. In the long term this is done by ensuring the correct level of investment in the network. In the short term the electricity network can be subject to damage, and potentially major disruption, by the weather. Storms caused by winter weather fronts, winter snow fall and lightning storms at any time of year can damage the electricity distribution network and result in customers' supply of electricity being interrupted. To mitigate the effects of these events weather forecasts are closely monitored and staff deployed in advance of foreseeable major weather events. Arrangements are in place to use resources from contractors and other electricity distribution network operators in the event of major interruptions and contracts are in place with suppliers of materials and services which can be brought into action at short notice in the event of severe weather.

Scottish Hydro-Electric Power Distribution Limited

Report of the Directors (continued)

2. Business Review (continued)

Key Performance Indicators

The following financial and operational key performance indicators are used by the Company in measuring performance:

Financial

a) Operating Profit (£M)

Year to March 2005	£101.5M
Year to March 2006	£103.1M
Increase (%)	1.6%

b) Capital Expenditure (£M)

Year to March 2005	£42.0M
Year to March 2006	£42.9M
Increase (%)	2.1%

Operational

c) Electricity Distributed (TWh)

Year to March 2005	8.7 TWh
Year to March 2006	8.9 TWh
Increase (%)	2.3%

d) Customer Minutes Lost

Year to March 2005	86
Year to March 2006	65
Reduction (%)	24.4%

e) Customer Interruptions – number per 100 customers

Year to March 2005	89
Year to March 2006	79
Reduction (%)	11.2%

3. Results and Dividends

The profit for the financial year amounted to £55.4m (2005 - £55.7m as restated). A final dividend of £21.0m (2005 - £24.0m) was declared during the year. The final dividends declared in 2005 and 2006 were paid in the year ended 31 March 2006.

Scottish Hydro-Electric Power Distribution Limited

Report of the Directors (continued)

4. Directors

The Directors who served during the year were as follows: -

Gregor Alexander
Colin Hood
Steven Kennedy

5. Directors' Interests in Ultimate Holding Company

The interests of Colin Hood and Gregor Alexander in the shares of the Company's ultimate holding company, Scottish and Southern Energy plc, are noted in the accounts of Scottish and Southern Energy plc. The interests of Steven Kennedy in Scottish and Southern Energy plc are as follows:

	31 March 2006		1 April 2005	
	No of shares beneficially held	**No of shares under option**	No of shares beneficially held	No of shares under option
Steven Kennedy	**1,322**	**4,836**	1,024	5,131

6. Political and Charitable Donations

During the year, no charitable or political donations were made.

7. Employment Policies

Staff are actively encouraged to be involved in Company affairs in a wide variety of ways. These include monthly team meetings, briefing documents and internal videos. Policies on such matters as Equal Opportunities and Health and Safety are regularly communicated to staff and involvement is supported through local committees. New staff joining the Company receive induction training.

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

8. Supplier Payment Policy

The Company complies with the CBI Prompt Payment Code. The main features of the Code are that payment terms are agreed at the outset of a transaction and are adhered to; that there is a clear and consistent policy that bills are paid in accordance with the contract; and that there are no alterations to payment terms without prior agreement. Copies of the Code are available on application to the Company Secretary. The number of suppliers' days represented by trade creditors was 30 days at 31 March 2006 (2005 - 30 days).

Scottish Hydro-Electric Power Distribution Limited

Report of the Directors (continued)

9. Auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware; and each director has taken all the steps that ought to have been taken as a director to be aware of any relevant audit information and to establish that the company's auditors are aware of that information.

ON BEHALF OF THE BOARD

Vincent Donnelly
Company Secretary
24 July 2006

Scottish Hydro-Electric Power Distribution Limited

Statement of directors' responsibilities in respect of the Directors' Report and the Accounts

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

Company law requires the directors to prepare Accounts for each financial year. Under that law they have elected to prepare the Accounts in accordance with UK Accounting Standards.

The Accounts are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing these Accounts, the directors are required to:

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

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that its Accounts comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

Scottish Hydro-Electric Power Distribution Limited

Independent Auditors' Report to the Members of Scottish Hydro-Electric Power Distribution Limited

We have audited the Accounts of Scottish-Hydro Electric Power Distribution Limited for the year ended 31 March 2006 which comprise the Profit and Loss Account, the Balance Sheet, the Statement of Total Recognised Gains and Losses and the related notes. These Accounts have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors
As described in the Statement of Directors' Responsibilities on page 5, the company's directors are responsible for the preparation of the Accounts in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

Our responsibility is to audit the Accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Accounts give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Accounts. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the Accounts, and of whether the accounting policies are appropriate to the company's circumstances, 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 Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Accounts.

Opinion
In our opinion:

- the Accounts give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 March 2006 and of its profit for the year then ended;
- the Accounts have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the Accounts.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
Edinburgh
24 July 2006

Scottish Hydro-Electric Power Distribution Limited

Profit and Loss Account
for the year ended 31 March 2006

	Note	2006 £M	2005 restated £M
Turnover		**208.9**	193.6
Cost of sales		**(23.4)**	(14.7)
Gross profit		**185.5**	178.9
Distribution costs		**(74.5)**	(66.7)
Administrative costs		**(7.9)**	(10.7)
Operating profit	3	**103.1**	101.5
Gains on disposal of fixed assets		**0.1**	0.1
Net interest payable	6	**(18.8)**	(19.8)
Profit on ordinary activities before taxation		**84.4**	81.8
Tax on profit on ordinary activities	7	**(29.0)**	(26.1)
Profit for the financial year	18	**55.4**	55.7

The above results are derived from continuing activities.

The accompanying notes are an integral part of these Accounts.

Scottish Hydro-Electric Power Distribution Limited

Balance Sheet
as at 31 March 2006

	Note	2006 £M	2005 restated £M
Fixed Assets			
Tangible assets	9	**706.8**	695.8
Current assets			
Stocks	10	**1.2**	1.1
Debtors:			
Amounts falling due within one year	11	**225.2**	199.8
Amounts falling due after more than one year	11	**28.0**	28.0
		254.4	228.9
Creditors			
Amounts falling due within one year	12	**(192.2)**	(165.0)
Net current assets		**62.2**	63.9
Total assets less current liabilities		**769.0**	759.7
Creditors:			
Amounts falling due after more than one year	13	**(455.0)**	(453.4)
Provisions for liabilities and charges			
Deferred taxation	15	**(146.3)**	(147.0)
Other provisions	16	**-**	(1.6)
Net assets		**167.7**	157.7
Capital and reserves			
Called up share capital	17	**62.0**	62.0
Profit and loss account	18	**105.7**	95.7
Equity shareholders' funds		**167.7**	157.7

These Accounts were approved by the Directors on 24 July 2006 and signed on their behalf by

Gregor Alexander, Director

Scottish Hydro-Electric Power Distribution Limited

Statement of Total Recognised Gains and Losses for the year ended 31 March 2006

	2006 £M	2005 restated £M
Profit for the financial year	**55.4**	55.7
Total recognised gains and losses relating to the financial year	**55.4**	55.7
Prior year adjustments (note 2)	**(55.0)**	
Total gains and losses recognised since last annual report	**0.4**	

Reconciliation of Movement in Shareholders' Funds as at 31 March 2006

	2006 £M	2005 restated £M
Profit for the financial year	**55.4**	55.7
Dividends	**(45.0)**	(17.0)
Credit in respect of employee share schemes	**0.3**	0.2
Purchase of shares to satisfy employee share awards	**(0.7)**	(0.2)
Net addition to shareholders' funds	**10.0**	38.7
Opening shareholders' funds	**157.7**	119.0
Closing shareholders' funds	**167.7**	157.7

The opening shareholders' funds at 1 April 2005 were originally £188.7m before prior year restatements of £31.0m (note 2).

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

1. Significant accounting policies

Basis of preparation
The Accounts have been prepared in accordance with all applicable United Kingdom accounting standards. The principal accounting policies are summarised below and have been applied consistently.

Under Financial Reporting Standard 1 (FRS 1), the Company is exempt from the requirement to prepare a cash flow statement on the grounds that the ultimate parent undertaking includes the Company in its own published consolidated Accounts.

As the Company is a wholly owned subsidiary of Scottish and Southern Energy plc (SSE plc), it has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the Scottish and Southern Energy Group (the Group).

The company has adopted a number of new accounting policies or has amended previous policies as a result of new accounting standards becoming applicable. In particular, the impact and applicability of the following standards should be noted:

- The presentation requirements of FRS 25 *Financial Instruments: Disclosure and Presentation*;
- The application of FRS 20 *Share based payments* has been restricted to equity instruments issued by the ultimate parent that were granted to employees of the company on or after 7 November 2002 and had not vested by 1 January 2005;
- FRS 21 *Events after the Balance Sheet Date*;
- FRS 28 *Corresponding amounts.*

The company has changed the accounting policy on the measurement of deferred taxation by ceasing to measure the provision for deferred tax on a discounted basis (note 2).

Turnover
Turnover comprises the value of electricity distribution services and facilities provided during the year. Turnover includes an estimate of the value of the distribution of electricity on behalf of customers between the date of the last meter reading and the year-end.

Research and development
Expenditure on research and development is charged to the profit and loss account as incurred.

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

1. Significant accounting policies (continued)

Taxation
The charge for taxation is based on the profit for the year and takes into account deferred taxation.

Current tax, including UK corporation 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 taxation arises in respect of all items where there are timing differences between their treatment for accounting and taxation purposes. This is recognised where an obligation to pay more tax in the future has originated but not reversed at the balance sheet date. A deferred tax asset is recognised only when 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.

Tangible fixed assets

(i) Depreciation
Heritable and freehold land is not depreciated.

Depreciation is provided on tangible fixed assets to write off cost, less residual values, on a straight-line basis over their estimated operational lives. The estimated operational lives are as follows:

	Years
Distribution assets	10 to 40
Non-operational assets:	
Buildings - freehold	Up to 60
- leasehold	Lower of lease period and 60
Fixtures, equipment, plant and machinery, vehicles and mobile plant	4 to 10

(ii) Subsequent expenditure
Expenditure incurred to replace a component of a tangible fixed asset that is accounted for separately is capitalised. Other subsequent expenditure is capitalised only when it increases the future economic benefits of the tangible fixed asset to which it relates.

Stocks and work in progress
Stocks are valued at the lower of cost and net realisable value. The valuation of work in progress is based on the cost of labour, plus appropriate overheads and the cost of materials. Progress invoices are deducted in arriving at the amounts stated

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

1. Significant accounting policies (continued)

Employee benefit obligations
Pensions
The Scottish and Southern Energy Group operates a number of pension schemes on behalf of employees. The amounts charged represent the contributions payable to the schemes in the year and are charged directly to the profit and loss account as incurred.

Equity and equity-related compensation benefits
Scottish and Southern Energy plc, the ultimate parent of the Company, operates a number of All Employee Share Schemes as described in the Remuneration Report of the Group. These schemes enable Group employees to acquire shares of the ultimate parent company. The employees of the Company are entitled, where applicable, to participate in these schemes. The Company has been charged with the cash cost of acquiring shares on behalf of its employees with a corresponding increase in the equity of Scottish and Southern Energy plc. Where the fair value of the options granted has been measured, the Company has recognised the expense as if the share based payments related to the Company's own shares.

Applying the transitional provisions of FRS 20, its requirements have been applied to all grants of equity instruments after 7 November 2002 that had not vested as at 1 January 2005.

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

The costs associated with the other main employee schemes, the share incentive plan and the deferred bonus scheme, are recognised over the period to which they relate.

Dividends on shares presented within shareholders' funds

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. Unpaid dividends that do not meet these criteria are disclosed in the notes to these accounts.

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

2. Prior year adjustments

The Company has changed the accounting policy on deferred tax to align it with the new group accounting policy. Previously, deferred tax was measured on a discounted basis. The change in accounting policy is to state deferred tax on an un-discounted basis. A prior year adjustment has been made in respect of this change in measurement basis, resulting in an increase in the tax charge and a reduction in the profit for 2005 of £1.5M. The deferred tax liability at 31 March 2005 has increased by £55.4M with a consequent reduction in net assets of £55.4M at that date. The adjustment has not affected the reported net assets at 31 March 2006.

As a result of the adoption of FRS 21 *Events after the Balance Sheet date*, a prior year adjustment has been made in respect of the recognition of proposed dividends. The adjustment has not affected the reported net assets at 31 March 2006, but has increased net assets at 31 March 2005 by £24.0M.

As a result of the introduction of FRS 20 *Share-based payment*, a prior year adjustment has been made in respect of the net share based credit in profit after tax in 2005 of £0.6M, with a consequent effect to increase net assets at 31 March 2005.

Summary

Profit attributable to shareholders:

	2005 £M
Adoption of FRS 20	
Credit to the profit and loss account	0.8
Net increase in profit before taxation	0.8
Tax on the adoption of FRS 20	
(Increased) tax charge	(0.2)
Change in the application of FRS 19	
(Increased) tax charge	(1.5)
Total net profit (decrease)	(0.9)
As previously reported	56.6
As restated	**55.7**

Net assets as at:

	2005 £M
Impact of FRS 20	
Increase in inter-company debtor	1.0
Increase in inter-company creditor	(0.4)
Corporation tax thereon	(0.2)
Impact of change in application of FRS 19	
(Increase) in provision for deferred tax	(55.4)
Impact of FRS 21	
Reduction in inter-company creditor	24.0
(Reduction) in net assets	(31.0)
As previously reported	188.7
As restated	**157.7**

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

3. Operating profit

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

	2006 **£M**	2005 restated £M
Depreciation of tangible fixed assets	**31.6**	30.8
Operating lease rentals	**0.5**	0.5
Release of deferred income in relation to customer contributions and capital grants	**(3.6)**	(3.0)
Gain on disposal of tangible fixed assets	**(0.1)**	(0.1)
Research and development	**0.3**	0.2
Net management fee in respect of services provided by group companies	**7.9**	7.1

The Company incurred an audit fee of £0.05m in the year (2005 - £0.06m).

4. Staff costs and numbers

	2006 **£M**	2005 restated £M
Staff costs:		
Wages and salaries	**23.2**	22.9
Social security costs	**2.1**	2.0
Share based remuneration	**0.3**	0.2
Other pension costs	**3.5**	3.5
	29.1	28.6
Less charged as capital expenditure	**(12.3)**	(13.5)
	16.8	15.1

Employee numbers

	2006 **Number**	2005 Number
Numbers employed at 31 March	**789**	825

	2006 **Number**	2005 Number
The monthly average number of people employed by the Company during the year:	**754**	787

5. Directors' remuneration

No Director received remuneration in respect of their service to the Company (2005 - nil).

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

6. Net interest payable

	2006 £M	2005 £M
Interest receivable:		
Other interest receivable	**9.1**	7.9
Interest payable:		
Bank loans and overdrafts	**(4.3)**	(4.3)
Other financing charges	**(23.6)**	(23.4)
	(27.9)	(27.7)
Net interest payable	**(18.8)**	(19.8)

7. Taxation

	2006 £M	2005 restated £M
Current tax:		
UK corporation tax	**29.7**	24.2
Deferred tax:		
Origination and reversal of timing differences	**(4.5)**	1.4
Adjustment in respect of prior years	**3.8**	0.5
Total Deferred Tax	**(0.7)**	1.9
Total tax on profit on ordinary activities	**29.0**	26.1

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

	2006 £M	2005 restated £M
Profit before tax	**84.4**	81.8
Tax on profit on ordinary activities at standard UK corporation tax rate of 30% (2005 - 30%)	**25.3**	24.5
Effects of:		
Capital allowances in excess of depreciation	**4.9**	(1.2)
Expenses not deductible for tax purposes	**-**	1.2
Other timing differences	**(0.4)**	(0.2)
Non-taxable income	**(0.1)**	(0.1)
Current tax charge for year	**29.7**	24.2

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

8. Dividends

	2006 **£M**	2005 restated £M
Amounts recognised as distributions from equity:		
Final dividend for the previous year of 38.71p (2005 – 27.42p) per share	**24.0**	17.0
Final dividend for the current year of 33.87p (2005 - nil) per share	**21.0**	-
	45.0	17.0
Proposed final dividend for the current year of nil (2005 – 38.71p) per share	**-**	24.0

The final dividend paid, £21.0m (33.87p, 2005 – 38.71p), was declared on 17 March 2006 and was paid to shareholders on 31 March 2006. The final dividend declared for 2005 was approved at the Annual General Meeting on 28 July 2005 and paid to shareholders on 23 September 2005.

9. Tangible fixed assets

	Distribution assets £M	**Other land and buildings £M**	**Vehicles and miscellaneous equipment £M**	**Total £M**
Cost:				
At 1 April 2005	1,101.6	6.1	62.0	1,169.7
Additions	42.3	-	0.6	42.9
Disposals	(0.4)	-	-	(0.4)
At 31 March 2006	1,143.5	6.1	62.6	1,212.2
Depreciation:				
At 1 April 2005	428.7	-	45.2	473.9
Charge for the year	25.6	-	6.0	31.6
Disposals	(0.1)	-	-	(0.1)
At 31 March 2006	454.2	-	51.2	505.4
Net book value:				
At 31 March 2006	**689.3**	**6.1**	**11.4**	**706.8**
At 31 March 2005	672.9	6.1	16.8	695.8

	2006 £M	2005 £M
Tangible fixed assets include:		
Assets in the course of construction	**3.6**	3.5

10. Stocks

	2006 £M	2005 £M
Raw materials and consumables	**1.2**	1.1

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

11. Debtors

	2006 £M	2005 restated £M
Amounts falling due within one year:		
Trade debtors	**12.9**	6.0
Amounts owed by group undertakings	**212.3**	193.8
	225.2	199.8
Amounts falling due after more than one year:		
Amounts owed by group undertakings	**28.0**	28.0
	253.2	227.8

12. Creditors: amounts falling due within one year

	2006 £M	2005 restated £M
Trade creditors	**2.6**	4.2
Loans due to ultimate parent (note 14)	**-**	100.0
Amounts owed to group undertakings	**152.8**	29.4
Corporation tax	**25.8**	19.0
Taxation and social security	**-**	1.2
Other creditors	**1.2**	1.3
Accruals and other deferred income	**9.8**	9.9
	192.2	165.0

13. Creditors: amounts falling due after more than one year

	2006 £M	2005 restated £M
Loans (note 14)	**75.0**	75.0
Loans due to ultimate parent (note 14)	**300.0**	300.0
Accruals and other deferred income	**74.4**	72.8
Amounts owed to group undertakings	**5.6**	5.6
	455.0	453.4

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

14. Analysis of borrowings

	Weighted Average Interest rate 2006 %	Weighted Average Interest rate 2005 %	**2006 £M**	2005 restated £M
Within one year				
Floating rate Loan Stock repayable to Scottish and Southern Energy plc on 31 March 2006	**-**	5.24	**-**	100.0
Over five years				
6.29% European Investment Bank repayable on 24 September 2012	**6.29**	6.29	**50.0**	50.0
Floating rate European Investment Bank repayable on 13 June 2014	**4.50**	4.88	**25.0**	25.0
5.90% Loan Stock repayable to Scottish and Southern Energy plc on 31 March 2022	**5.90**	5.90	**300.0**	300.0
			375.0	375.0
			375.0	475.0

15. Deferred Taxation

Deferred taxation is provided as follows:

	2006 £M	2005 restated £M
Accelerated capital allowances	**146.5**	147.7
Other timing differences	**(0.2)**	(0.7)
Provision for deferred tax	**146.3**	147.0

	31 March 2006
Provision at 31 March 2005 as previously stated	91.6
Prior year adjustment (note 2)	55.4
Provision at 31 March 2005 as restated	147.0
Transferred from / (to) profit and loss account	(0.7)
Provision at 31 March 2006	**146.3**

16. Provisions for liabilities and charges

	Restructure £M
At 1 April 2005	1.6
Released in the year	(1.6)
At 31 March 2006	**-**

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

17. Share capital

	2006	2005
	£	£
Equity:		
Authorised:		
62,001,000 ordinary shares of £1 each	**62,001,000**	62,001,000
Allotted, called up and fully paid:		
62,000,000 ordinary shares of £1 each	**62,000,000**	62,000,000

18. Reserves

	Profit and loss account £M
At 31 March 2005	126.7
Prior year adjustments (note 2)	(31.0)
At 31 March 2005 restated	95.7
Retained profit for the year	55.4
Dividends to shareholders	(45.0)
Credit in respect of employee share awards	0.3
Purchase of shares to satisfy employee share awards	(0.7)
At 31 March 2006	**105.7**

19. Pensions

The majority of the Company's employees are members of the Scottish Hydro-Electric Pension Scheme which provides defined benefits based on final pensionable pay. The Company's contributions to this scheme are set in relation to the current service period only (i.e. these are not affected by any surplus or deficit in the scheme relating to past service of its own employees and any other members of the scheme) and as such are treated as contributions to a defined contribution scheme.

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

The Company's share of the total contribution payable to the pension schemes during the year was £3.5m (2005 - £3.5m).

20. Employee share-based payments

The Group operates a number of share schemes for the benefit of all employees. Details of these schemes are as follows:

(i) Savings-related share option schemes ("Sharesave")

This scheme gives employees the option to purchase shares in the parent Company at a discounted market price, subject to them remaining in employment with the Group for the term of the agreement. Employees may opt to save between £5 and £250 per month for a period of 3 or 5 years and at the end of this period, employees have six months to exercise their options by using the cash saved (including a bonus equivalent to interest). If the option is not exercised, the funds may be withdrawn by the employee and the option expires.

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

20. Employee share-based payments (continued)

(ii) Share Incentive Plan (SIP)
This scheme allows employees the opportunity to purchase shares in the parent Company on a monthly basis. Employees may nominate an amount between £10 and £125 to be deducted from their gross salary, and this is then used to purchase shares (‘partnership shares’) in the market on the final business day of each month. These shares are then held in trust for a period of 5 years, at which point they are transferred at no further cost to the employee. These shares may be withdrawn at any point during the 5 years, but tax and national insurance would then be payable on any amounts withdrawn.

In addition to the shares purchased on behalf of the employee, the Group will match the purchase up to a maximum of 5 shares (‘matching shares’) per month. Again these shares are held in trust for the five years until they are transferred to the employee. If an employee leaves during the first three years, or removes his/her ‘partnership’ shares, these ‘matching’ shares are forfeited.

In addition to the above, at 31 March 2005 the Group made a special award of 50 free shares to all employees in employment at both 31 March and 20 August 2005 in recognition of their contribution to the success of the Group. Under the arrangements for the award, the shares will be held in trust for five years, at which point they will be transferred to the employees at no cost to the employee. These shares may be withdrawn by the employee at any point during years four and five, but tax and national insurance would then be payable on any amounts withdrawn.

(iii) Deferred bonus scheme
This scheme applies to approximately 70 senior managers and executive directors. Those eligible are awarded an amount equal to their cash bonus for the period which is adjusted by a multiplier of between 0.7 and 1.35 depending on three factors, namely: relative performance in terms of Total Shareholder Return (TSR) over a three year period compared to the FTSE100; safety; and relative performance in terms of customer complaints (as recorded by energywatch). This amount is then used to purchase shares of the parent company in the market which are held in trust on behalf of the employee for a period of three years, at which point the employee is entitled to exercise the award. In addition to shares purchased using the adjusted bonus award, additional shares will also be purchased using any dividends received on the shares held by the trust. If the employee resigns, they will lose all outstanding awards.

As allowed by FRS 20, only options granted since 7 November 2002, which were unvested at 1 January 2005, have been included.

Details used in the calculation of these costs are as follows:

(i) Savings-related share option scheme

Date of grant		25 July 2003		16 July 2004		14 July 2005	
		2006	2005	**2006**	2005	**2006**	2005
Outstanding at start of year	Shares	**260,732**	279,677	**172,628**	-	**-**	-
	Price	***562***	*562*	***622***	-	**-**	-
Granted	Shares	**-**	-	**-**	174,144	**164,361**	-
	Price	**-**	-	**-**	*622*	***886***	-
Forfeited	Shares	**(6,958)**	(18,648)	**(4,310)**	(1,516)	**(7,632)**	-
	Price	***562***	*562*	***622***	*622*	***886***	-
Exercised	Shares	**(218)**	(297)	**(45)**	-	**-**	-
	Price	***986***	*728*	***930***	-	**-**	-
Outstanding at end of year	Shares	**253,556**	260,732	**168,273**	172,628	**156,729**	-
	Price	***562***	*562*	***622***	*622*	***886***	-

Of the outstanding options at the end of the year, none were exercisable.

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

20. Employee share-based payments (continued)

(i) Savings-related share option scheme (continued)

The fair value of these shares at vesting, calculated using the Black-Scholes model, and the assumptions made in that model are as follows:

	July 2003		July 2004		July 2005	
	3 Year	5 Year	3 Year	5 Year	3 Year	5 Year
Price	659p	667p	730p	739p	1,012p	1,023p
Expected volatility	17%	17%	17%	17%	15%	15%
Risk free rate	4.7%	4.8%	4.7%	4.8%	4.1%	4.2%
Expected dividends	4.6%	4.6%	4.6%	4.6%	4.2%	4.2%
Term of the option	3 yrs	5 yrs	3 yrs	5 yrs	3 yrs	5 yrs
Underlying price at grant date	630p	630p	699p	699p	967p	967p
Strike price	562p	562p	622p	622p	886p	886p

Expected price volatility was obtained by calculating the historical volatility of the Group's share price over the previous 12 months.

In addition to the sharesave schemes detailed above, at 31 March 2006 there were outstanding options under the 2001 sharesave issue. Since the shares under this scheme were granted prior to 7 November 2002, they have not been included as permitted by the transitional rules under FRS 20. However, at 31 March 2006, the outstanding options are as follows:

Date of grant	Number at 31 March 2006	Price (pence)	Date from which exercisable	Expiry date
October 2001	164,354	566	December 2006	May 2007

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

20. Employee share-based payments (continued)

(ii) Share Incentive Plan

	2006 Shares	**2006** Weighted average price (pence)	2005 Shares	2005 Weighted average price (pence)
Outstanding at start of year	**49,086**	**716**	26,273	632
Granted	**28,407**	**1,028**	24,027	803
Forfeited	**(2,243)**	**716**	(1,214)	632
Exercised	**(420)**	**1,084**	-	-
Outstanding at end of year	**74,830**	**834**	49,086	716

Of the outstanding options at the end of the year, none were exercisable.

Shares purchased under this scheme prior to 7 November 2002 have not been included as permitted by the transitional rules under FRS 20.

Free shares

	2006 Shares	**2006** Weighted average price (pence)	2005 Shares	2005 Weighted average price (pence)
Outstanding at start of year	**-**	**-**	-	-
Granted	**38,200**	**965**	-	-
Forfeited	**(700)**	**965**	-	-
Exercised	**(150)**	**1,057**	-	-
Outstanding at end of year	**37,350**	**965**	-	-

Of the outstanding options at the end of the year, none were exercisable.

(iii) Deferred bonus scheme

	2006 Shares	**2006** Price (pence)	2005 Shares	2005 Price (pence)
Outstanding at start of year	**6,333**	**653**	3,386	626
Granted	**4,784**	**1,009**	2,947	685
Outstanding at end of year	**11,117**	**811**	6,333	653

Of the outstanding options at the end of the year, none were exercisable.

Shares purchased under this scheme prior to 7 November 2002 have not been included as permitted by the transitional rules under FRS 20.

Scottish Hydro-Electric Power Distribution Limited

Notes on the Accounts
for the year ended 31 March 2006

21. Commitments and contingencies

(i) Capital commitments

Capital expenditure

	2006	2005
	£M	£M
Contracted for but not provided	**8.2**	3.0

(ii) Operating lease commitments

The payments under operating leases which are due to be made in the next year, analysed over the periods when the leases expire, are:

	Other assets	
	2006	2005
	£M	£M
After five years	**0.4**	0.5

(iii) Guarantees

The Company has provided a guarantee in relation to £450m Eurobonds held by Scottish and Southern Energy plc. This guarantee has been provided jointly with Scottish Hydro-Electric Transmission Limited.

22. Ultimate parent company

The Company is a subsidiary of Scottish and Southern Energy plc, a company registered in Scotland, whose consolidated accounts (which include those of the Company) are available from Corporate Communications, Inveralmond House, 200 Dunkeld Road, Perth PH1 3AQ.

Scottish Hydro-Electric Power Distribution Limited

Additional Disclosures: Regulatory Financial Statements

The attached schedules represent additional information required by Standard Condition 42 of the Electricity Distribution Licence.

This includes a Cash Flow Statement and additional guidance on the accounting policies adopted.

Scottish Hydro-Electric Power Distribution Limited

Cash Flow Statement
for the year ended 31 March 2006

	Note	**2006 £M**	2005 £M
Net cash inflow from operating activities	(i)	**230.3**	96.7
Returns on investments and servicing of finance	(ii)	**(18.8)**	(19.8)
Taxation		**(22.9)**	(19.9)
Free cash flow		**188.6**	57.0
Capital expenditure and financial investment	(iii)	**(43.6)**	(40.0)
Equity dividends paid		**(45.0)**	(17.0)
Net cash inflow before management of liquid resources and financing		**100.0**	-
Financing	(iv)	**(100.0)**	-
Increase in cash* in the year		**-**	-

Notes to the Cash Flow Statement
for the year ended 31 March 2006

Reconciliation of net cash flow to movement in net debt

	2006 £M	2005 £M
Cash inflow from increase in cash*	**-**	-
Cash outflow from decrease in debt and lease financing	**100.0**	-
Movement in net debt in the year	**100.0**	-
Net debt at 1 April	**(475.0)**	(475.0)
Net debt at 31 March	**(375.0)**	(475.0)

Analysis of net debt

	As at 1 April 2005 £M	Increase in cash* £M	(Increase)/ decrease in debt £M	**As at 31 March 2006 £M**
Cash at bank and in hand	-	-	-	
Other debt due within one year	-	-	-	
Net borrowings due within one year	-	-	-	
Net borrowings due after more than one year	(475.0)	-	100.0	**(375.0)**
Net debt	(475.0)	-	100.0	**(375.0)**

* The Company does not hold cash balances at any time. Cash generated or required by the Company is remitted to or obtained from SSE Services plc. As a result the movement in increase of the indebtedness from the Group can be said to represent the cash generated in the year.

Scottish Hydro-Electric Power Distribution Limited

Notes to the Cash Flow Statement (continued)
for the year ended 31 March 2006

		2006 £M	2005 £M
	Reconciliation of operating profit to operating cash flows		
	Operating profit	**103.1**	101.5
	Depreciation	**31.6**	30.8
	Customer contributions and capital grants released	**(3.6)**	(3.0)
	(Increase) in stocks	**-**	(1.4)
	(Increase) in debtors	**(6.9)**	(30.1)
	Increase/(decrease) in creditors	**106.5**	(0.2)
	(Decrease) in provisions	**-**	(0.7)
	Employee share award share purchase	**(0.7)**	(0.4)
	Charge in respect of employee share awards	**0.3**	0.2
(i)	**Net cash inflow from operating activities**	**230.3**	96.7
	Returns on investments and servicing of finance		
	Interest received	**9.1**	7.9
	Interest paid	**(27.9)**	(27.7)
(ii)	**Net cash (outflow) from returns on investments and servicing of finance**	**(18.8)**	(19.8)
	Capital expenditure and financial investment		
	Purchase of tangible fixed assets	**(43.9)**	(40.1)
	Sale of tangible fixed assets	**0.1**	0.1
(iii)	**Net cash (outflow) from capital expenditure and financial investment**	**(43.8)**	(40.0)
	Financing		
	Repayment of borrowings	**(100.0)**	-
(iv)	**Net cash inflow from financing**	**(100.0)**	-

Scottish Hydro-Electric Power Distribution Limited

Notes on the Regulatory Financial Statements for the year ended 31 March 2006

1. Principal accounting policies

Basis of accounting

The Regulatory Financial Statements have been prepared under the historical cost convention and in accordance with UK generally accepted accounting standards (UK GAAP) and as required by Standard Condition 42, Regulatory Accounts, of the Electricity Distribution Licence. The principal accounting policies are summarised in the Notes to the Accounts and have been applied consistently.

Limitation of application of CA85 exemption disclosure

Standard Condition 42 requires the Regulatory Financial Statements to be prepared inclusive of all mandatory disclosures which otherwise may have been excluded from the Statutory Accounts as a result of the application of a CA85 exemption allowance.

However, as the Company is a wholly owned subsidiary of Scottish and Southern Energy plc ("the Group"), the Directors believe certain accounting policies required of listed Companies cannot practicably be applied to the Company. These include, but are not limited to:

- Pensions. The Group operates three Defined Benefit Schemes, one of which, the Scottish Hydro-Electric Pension Scheme, is the main Pension Scheme for the Company. The contributions made to this scheme are treated as contributions to a Defined Contribution scheme. The Defined Benefit Schemes disclosure is published in the accounts of the Group. The Pensions accounting policy is commented upon in the notes to the accounts.

- Director's Remuneration. The remuneration of the Directors of the Company who are also Executive Directors of the Ultimate Parent is published in the accounts of the Group

Furthermore, while it has been mandatory to prepare financial statements of listed entities in accordance with EU-adopted International Financial Reporting Standards (adopted IFRS) for reporting periods beginning on or after 1 January 2005, the statutory accounts of all the Group's subsidiary entities continue to be prepared under UK GAAP. As a result, the Directors of the Company, and those of the Group, do not believe it would be reasonably practicable to prepare the Regulatory accounts of the Company under adopted IFRS.

Independent auditors' report to Scottish Hydro-Electric Power Distribution Limited and to the Chairman of OFGEM ("The Regulator")

We have audited the Regulatory Accounts of Scottish Hydro-Electric Power Distribution Limited ("the Company") set out in section 2 on pages 7 to 27 which comprise: the profit and loss account, balance sheet, statement of recognised gains and losses, cash flow statement and the related notes to the Regulatory Accounts. These Regulatory Accounts have been prepared under the accounting policies set out therein.

This report is made, on terms that have been agreed, solely to the Company and the Regulator in order to meet the requirements of Condition 42 of the Company's 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 company's 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 Accounts have been prepared under the historical cost convention and in accordance with Condition 42 of the Regulatory Licence and the accounting policies set out in the statement of accounting policies.

The Regulatory Accounts are separate from the statutory financial statements of the Company. There are differences between United Kingdom Generally Accepted Accounting Principals (UK GAAP) and the basis of preparation of information provided in the regulatory accounts because the Condition 42 of the Regulatory Licence specify alternative treatment or disclosure in certain respects. Where Condition 42 of the Regulatory Licence does not specifically address an accounting issue, then it requires UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of the company as shown in financial statements prepared in accordance with the Companies Act 1985.

Respective responsibilities of the regulator, the directors and auditors

The nature, form and content of Regulatory Accounts 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 assessment.

As described in the Statement of Directors' Responsibilities in section 2 on page 5, the Company's directors are responsible for the preparation of the Regulatory Accounts in accordance with Condition 42 of the Regulatory Licence.

Our responsibility is to audit the Regulatory Accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland), except as stated in the "Basis of audit opinion", below and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities'.

We report to you our opinion as to whether the regulatory accounts present fairly in accordance with Condition 42 of the Regulatory Licence and the accounting policies set out in section 2 on page 27, the results, cash flows and financial position of the Company and whether they have been properly prepared in accordance with those conditions. We also report to you if, in our opinion, the Company has not kept proper accounting records or if, in our opinion, we have not received all the information and explanations we require for our audit.

We read the other information contained in the Regulatory Accounts, 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 misstatements or material inconsistencies with the Regulatory Accounts. The other information comprises the Corporate Report, review of the year and Corporate Governance Statement. Our responsibilities do not extend to the other information.

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 Accounts. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Regulatory Accounts, and of whether the accounting policies are appropriate to the company's circumstances, 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 Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Regulatory

Independent auditors' report to Scottish Hydro-Electric Power Distribution Limited and to the Chairman of OFGEM ("The Regulator") (continued)

Basis of audit opinion (continued)

Accounts 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 those auditing standards.

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory accounts of the company on which we report, 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 those matters which we are required to state to them in a statutory auditors' 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'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 Accounts of the company for the year ended 31 March 2006 fairly present, in accordance with Condition 42 of the Regulatory Licence and the accounting policies set out in section 2 on page 27, the state of the company's affairs at 31 March 2006 and of its profit and cash flows for the year and have been properly prepared in accordance with those conditions.

KPMG Audit Plc
Chartered Accountants
Edinburgh