

REGISTERED NUMBER: 05167021

Southern Gas Networks Plc

Strategic Report, Directors' Report and

Audited Financial Statements for the Year Ended 31 March 2021

Southern Gas Networks Plc (Registered number: 05167021)

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for the Year Ended 31 March 2021

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Southern Gas Networks Plc

Company Information
for the Year Ended 31 March 2021

DIRECTORS:

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Charlotte Brunning
Paul Jeffery
Guy Lambert
Robert McDonald
Charles Thomazi (Alternate)
Nicholas Robin Salmon (Chair)
Laura Sandys
Peter Mccosker (Alternate)
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Delphine Voeltzel

SECRETARY:

Nicola Shand

REGISTERED OFFICE:

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REGISTERED NUMBER:

05167021

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London
SE1 2AF

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Strategic Report
for the Year Ended 31 March 2021

The directors present their strategic report for the year ended 31 March 2021.

This strategic report sets out the main trends and factors underlying the development and performance of Southern Gas Networks Plc ("the Company") during the year ended 31 March 2021 as well as those matters which are likely to affect our future development and performance.

THE BUSINESS, ITS OBJECTIVES AND STRATEGY

The Company operates the regulated gas transportation business for the South and South East of England gas distribution network, one of eight regional gas distribution networks in Great Britain. Its gas distribution network comprises approximately 49,000 kilometres of gas mains delivering natural gas to approximately 4.0 million domestic, commercial and industrial customers. The network stretches from Milton Keynes in the north, to Dover in the east and Lyme Regis in the west, including London boroughs to the south of the River Thames.

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks Limited ("**SGN**"), which is registered at St. Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ. SGN is owned by a consortium made up of SSE plc, Borealis Infrastructure Europe (UK) Limited, which is indirectly wholly owned by OMERS Administration Corporation, OTPPB Investments (U.K.) Limited, which is owned by Ontario Teachers' Pension Plan Board and Blue Spyder B 2016 Limited, which is owned by Abu Dhabi Investment Authority. References to the "**Group**" throughout this Report mean SGN and its subsidiaries (including the Company).

The Company's business is regulated by the Office of Gas and Electricity Markets ("Ofgem").

Objectives and Strategy

The Company's principal objectives are to deliver natural gas safely, reliably and efficiently across the gas distribution network and to provide the highest standard of service to our stakeholders, whilst delivering value to our shareholders. Its strategy therefore places the highest emphasis on ensuring activities are carried out safely and that the networks operate in a reliable and efficient manner, so that benchmarks and regulatory targets can be exceeded to the benefit of all its stakeholders.

The Company's overall financial objective is to focus on operational efficiency and the efficient delivery of capital and replacement expenditure programmes. Therefore, financial objectives are set to ensure the regulatory targets are achieved or outperformed.

The Company's financing objective is to ensure an efficient capital structure that mitigates interest rate risk through maintaining a minimum of 75% of debt at either fixed rates of interest or index linked.

Our purpose is to keep everyone safe and warm. Our strategy is to deliver long-term value for existing and future customers, stakeholders and shareholders. This strategy is based on strong financial management and a governance framework, and underpinned by our detailed Business Plan and Strategic Pillars, summarised as follows:

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1. Safe and efficient

We will deliver a safe and efficient service by acting safely, keeping the gas flowing and keeping costs down.

2. Positive impact

We will make a positive impact on society, by supporting vulnerable communities and providing excellent service.

3. Shared future

We will build a shared net-zero future by accelerating decarbonised energy solutions and minimising our environmental impact.

4. Creating value

We will create value by accelerating commercial opportunities which complement the core; maximise the value from our existing asset base; invest in opportunities for the sustainability of our network and keep SGN at the forefront of the delivery of heat.

5. Our people

We will create and maintain an inclusive and diverse workplace where our people can develop and thrive.

External and regulatory environment

The management and operation of the Company's gas transportation assets are subject to a series of legislative requirements to ensure that assets are managed and operated in a safe and reliable manner. The Company must also ensure that arrangements are in place to respond to emergency situations and to ensure hazardous work is carried out safely and with minimum disruption.

The primary legislation controlling the Company's activities as a gas transporter is the Gas Act 1986 (as amended). Under the Gas Act, the Company holds a licence that allows it to operate the gas distribution network it owns. The Company is regulated by Ofgem, which has established price control mechanisms that govern the amount of revenue that can be earned by regulated businesses. Ofgem assesses the revenue and investment plans of the Company to determine an efficient level of expenditure and the quality of service requirements for the network are also taken into account. A cost of capital for the required investment in the networks is also determined.

The Company is also subject to safety legislation which is enforced by the Health and Safety Executive ("HSE") in the UK. The Group's processes and procedures are covered in a safety case which has been accepted by the HSE.

Factors affecting the business

The Company's principal activity is the operation of a highly complex gas infrastructure network. As a consequence, there are a number of factors that may influence the development and performance of the Company and the financial returns that can be achieved. The principal factors that influence the Company are as follows:

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- **Regulatory price controls**

The prices that can be charged for the use of the Company's networks are determined in accordance with regulator approved price controls. The year ended 31 March 2021 is the final year of the current RII01 price control. The key elements of revenue, outputs and allowed returns for the next five years have been set by the Regulator for RII0-GD2, although these are subject to ongoing CMA appeals.

Additionally, the regulatory price controls include an allowed rate of return for the investment the Company makes in the network. The allowed rate of return represents the return on debt and equity capital.

- **Safety and reliability of the networks**

The Company's ability to operate the networks safely and reliably is of the highest importance. Its performance in these areas affects the costs it incurs and the overall financial performance.

- **Efficiency**

The Company's objective is to ensure that gas is delivered as efficiently as possible through its network. This allows the Company to limit price increases and improve its own financial performance.

- **Interest rates**

The costs of financing our operations are affected by changes in interest rates as some of the Company's borrowings are held at floating rates. Exposure to changes in interest rates are hedged by holding both fixed rate and index linked borrowings and by holding derivative financial instruments (interest rate swaps) where necessary to achieve the desired profile of interest rate risk.

Southern Gas Networks Plc (Registered number: 05167021)Strategic Report
for the Year Ended 31 March 2021**PRINCIPAL RISKS AND UNCERTAINTIES**

As well as the opportunities the Company has to grow and develop its business, certain risks and uncertainties are faced in achieving its objectives. The principal risks and uncertainties identified are as follows:

Description and Impact of Risk	Mitigation
1. Future of gas network: Decisions from government on climate change present a risk to SGN due to the desired outcome being one that does not rely on gas network assets.	<p>Influencing government policy and regulatory decisions by setting up of a collaborative body of networks, industry, BEIS, and Ofgem.</p> <p>Co-ordination of the Hydrogen programme evidence and activity through the Energy Networks Association.</p> <p>Developing a clear SGN policy framework and plan for heat decarbonisation including hydrogen, biomethane, and heat networks.</p> <p>Utilising innovation funding and working with others to test potential decarbonisation pathways.</p>
2. Cyber and IT resilience: Failure to implement appropriate security risk management and crisis management could result in cyber-attacks from nation states, hactivists, criminals, and/or insiders.	<p>Secured uplift in Cyber security funding to combat risk.</p> <p>Developed a managed security service with an external partner to complement a skilled in-house security team to improve the defensive capability of our organisation.</p>
<p>Loss of critical IT services due to the design of core services and/or ineffective Business Continuity Management plans. Loss of IT services could result in interruption or disruption to our core business operations.</p>	<p>Working closely with our industry peers and government agencies to shape our delivery of the security programme as well as complying with the directives.</p> <p>Ongoing work to maintain business continuity and disaster recovery procedures focusing on consequences of geo-political actors or malicious activity.</p> <p>Hardware and Network resilience/segmentation in place.</p> <p>Maintenance plan and activities in place to manage the risk of failure.</p>
3. Political and public policy: There is a risk that adverse future intervention by the UK and Scottish Governments in the energy markets, or changes in governmental policy, may have an unfavourable impact on our business model.	<p>Contributing to development of UK and Scottish Government policy during 2021.</p> <p>Continue to build capability within the Company to promote our brand and explain our role.</p>

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4. Leadership, people and culture:

Failure to maintain a sufficiently competent, diverse and productive workforce with effective relationships and enough talent.

Also, the failure of the leadership team to recognise the changing external, internal environment and indifference to business risks.

Continuous development of our people with right skills and knowledge to deliver business objectives. Training and personal development exists for all employees in addition to talent management programmes.

We are developing change and training to support better, faster and more cost-effective operations.

We keep a close eye on and respond to regulatory, supplier, and technology developments that could have an impact on our strategic objectives.

5. Safety and Health: Failures in the design or implementation of the safety and health management systems may result in unsafe behaviour and working practices.

We have a continued focus on safety across all assets and operations.

We track a range of safety metrics very closely and have programmes in place to drive improvements.

We review lessons learnt from major incidents in order to prevent such things from recurring.

Compliance is supported by independent inspections and an audit programme.

We run wellbeing programmes and campaigns for our people.

6. Financing: The risk that the group is unable to, or that it costs the group materially more to raise equity or external debt financing to refinance existing debt or to fund further investment within the group.

The group has a treasury policy that is focused on maintaining:

- 12-18 months committed sources of liquidity (cash and committed facilities) within the group;
- A smooth debt maturity profile to minimise annual refinancing requirements and spread refinancing risk;
- Access to diversified sources of funding to avoid over-reliance on any one market;
- A proportion of direct or synthetic inflation debt liabilities to hedge the group's assets and cash flows.

Regular dialogue and updates provided to credit rating agencies.

Regular internal monitoring and reporting of key credit metrics and financial covenants to the Executive Committee, Finance Committee and Board.

SGN has identified a number of technical issues in Ofgem's RIIO GD2 final determination and, as a result, has referred these to the Competition and Market

Authority (CMA), for judgement. The areas that SGN has specifically appealed on include the cost of equity, outperformance wedge and certain aspects of Ofgem's efficiency methodology.

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7. Environment and climate adaption:

As we move to a zero-carbon economy there is a risk of failing to assess and manage changes as a result of weather, climate, zero carbon legislation and technological change.

Delivering the Environmental Action Plan and Environmental Sustainability Strategy by decarbonising the network and operations.

Engaging with the supply chain.

Delivering regular interaction with stakeholders and customers, including the establishment of an Environment Advisory Panel.

Full implementation of behavioural and cultural improvement.

Maintaining our ISO14001 accreditation.

8. Legal and compliance: Legal risk is the risk of financial or reputational loss that can result from lack of awareness or misunderstanding of, or ambiguity in, the way law and regulation apply to your business, its relationships, processes, products and services.

We are progressing programmes to strengthen our compliance framework, supported by relevant training for those in high risk roles.

We have policies covering controls including conflicts of interests, gifts and hospitality, money laundering and antibribery.

Our contracts include anti-corruption and bribery clauses.

We have rules and training to guide and support our people to protect the personal data they handle.

9. Supply chain: The risk of disruption to supply continuity if there is over-dependence on a limited number of suppliers and/or failure to meet increased expectations for sustainable procurement due to lack of lack of co-ordination with supplier partners.

Developing and harnessing new suppliers to encourage competition and innovation.

Supplier performance management and compliance across key areas.

Ongoing support and management of contracts to maximise commercials for both parties.

Preparation to deal with short term and long-term shocks.

10. Network asset management and physical security: Failures in the design and/or implementation of our asset management policy, management and security systems and procedures, or ineffective crisis management causing reputational damage and shareholder dissatisfaction.

Core business processes help ensure that gas supply to the customer is maintained.

Long-term horizon scanning is in place to capture network asset changes.

There is robust annual audit programme and site inspections to ensure compliance with our policies and procedures.

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We track a range of asset and safety related metrics very closely and have programmes in place to drive improvements.

We test resiliency through a number of activities such as emergency exercises and risk assessment tools.

Physical security upgrade program is designed to meet government agencies guidelines.

11. Customer interests: Failure to maintain high levels of customer service, in particular with our most vulnerable customers, could lead to financial penalties, reputational damage, business stagnation and loss of trust with a range of stakeholders from local communities to national government.

The new CXGD2 (Customer Experience GD2) project was signed off by the Executive in March 2021.

The company-wide vulnerability strategy was agreed by our VSG (Vulnerable stakeholder group) in March 2021 to harness new suppliers and to encourage competition and innovation in the area of vulnerability.

Ongoing support and management of external relationships to maximise collaboration and co-operation of all partners.

12. Licence conditions and regulatory requirements: Failure to comply with our licence conditions and obligations.

We have governance and compliance frameworks in place to deal with issues and developments arising from price controls.

Our experienced regulation, finance and legal teams manage compliance requirements and engage with all levels of Ofgem and Government.

Delivery of regulatory outputs is measured and monitored on a regular basis.

Annual Compliance report.

The Board reviews the principal risks and uncertainties facing the business and considers the risk management processes in place, which are designed to safeguard assets and to manage, rather than eliminate, material risks to the achievement of business objectives. These reviews recognise that any such process can provide only reasonable, and not absolute, assurance against material misstatement or loss. Further details of the processes the Board has in place are also set out in the Corporate Governance Statement, in the Directors' Report.

Stakeholders

The Company has a range of external stakeholders including gas consumers, employees, suppliers and contractors, its regulator Ofgem, the HSE and local governments and communities. The Company adopts an open and constructive approach, both in terms of the way it operates, the services it provides and the impact that its activities have on each of its stakeholders. The Company encourages and enables its employees to be active citizens in the communities in which they live and work, through schemes which support staff who are either raising money for, or giving their time to, UK charities, local community or youth sports groups. The Company matches eligible fund raising by individual members of staff.

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SECTION 172(1) STATEMENT

The Companies (Miscellaneous Reporting) Regulations 2018 require Directors to explain how they considered the interests of key stakeholders and the broader matters set out in section 172(1) (A) to (F) of the Companies Act 2006 ('S172') when performing their duty to promote the success of the Company under S172. In particular, how they have considered the long-term success of the company whilst balancing the interests of a wide range of stakeholders.

Confirmation of Directors' duties

The Company's Directors strive to ensure that they act in good faith, in promoting the future success of the Company, and in doing so having regard (among other matters) to:

S172(1) (A) "The likely consequences of any decision in the long-term"

The Directors' role is to promote the long-term success of the Company through the setting of a clear purpose, vision and sustainable strategy which creates value for existing and future customers, stakeholders and shareholders.

The Board have provided continued focus on the long-term success of the Company through setting its' vision, purpose and strategic priorities now, through the next price control, and beyond. These are all outlined further in the points below and throughout the Strategic and Directors' Report.

S172(1) (B) "The interests of the company's employees"

The Directors place considerable value on the involvement of its employees. It has continued to keep them informed on matters affecting them and on the various factors affecting the Company. Throughout the year the Directors have regularly invited employees to share their views at board dinners and through site and office visits. This culture continues with senior management and the CEO and other senior executives regularly communicating with employees through these channels and employee representatives are consulted regularly on a wide range of matters affecting their current and future interests.

Several of the Board's sub-committees have a high degree of focus on employee's interest, for example the Safety, Health and Environmental Advisory Committee which recognises that the health and safety of the Company's staff (as well as the other key stakeholders) are of critical importance. The People and Reward Committee also considers the appropriateness and relevance of the remuneration policy.

The Directors recognise that our pensioners, though no longer employees, also remain important stakeholders.

S172(1) (C) "The need to foster the company's business relationships with suppliers, customers and others"

The Directors' have taken steps to ensure everyone has an opportunity to share their views about what matters to them with the Company.

We have well-established customer engagement channels ranging from dedicated panels and focus groups to ensure perspectives of vulnerable customers are considered, to forums to engage with large business customers. Customer satisfaction surveys drive KPIs which measure how successful we are and provide feedback on the impact of our decisions. We use consumer research groups to engage and shape the key decisions we make. We use social media and our website to communicate directly with our customers. The Consumer Engagement Group (CEG) and Stakeholder Advisory Panel (SAP) help shape our engagement strategy by providing independent challenge on the use of our customer engagement in our business planning.

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The Company has used the valuable insight gathered from our customers and stakeholders to shape our business, and now structure our activities to align with the customer and stakeholder-driven commitments:

- We will make a positive impact on society, by supporting vulnerable communities and providing excellent service.
- We will deliver a safe and efficient service by acting safely, keeping the gas flowing and keeping costs down.
- We will build a shared net-zero future by accelerating decarbonised energy solutions and minimising our environmental impact.
- We will create value by accelerating commercial opportunities which complement the core; maximise the value from our existing asset base; invest in opportunities for the sustainability of our network and keep the Company at the forefront of the delivery of heat.

We work closely with suppliers as well to ensure their values on issues, such as, safety, environment and modern slavery are upheld throughout our supply chain. Meetings are held with strategic suppliers through our Supplier Relationship Management (SRM) programme, helping enhance performance and strengthen relationships to deliver mutual value as well as key relationship meetings with our Executive and CEO. To ensure high operational standards onsite health and safety audits are undertaken. We actively engaged with key suppliers to ensure we had sufficient stocks of key materials in preparation for Brexit and to support Covid-19 resilience.

S172(1) (D) "The impact of the company's operations on the community and the environment"

Working with communities at local, regional and national levels enables us to build our shared net-zero future by accelerating decarbonised energy solutions and minimising our environmental impact.

We held a number of consultation events and stakeholder workshops throughout the year to gather feedback on projects and business plans, and progressed partnerships with NGOs which deliver additional social and environmental benefits for the communities in which we operate.

The engagement throughout 2020/21 continued to build on the work undertaken within our communities including focused community engagement around our Replacement programme.

Using Stakeholder feedback, we have developed our Environmental Strategy and Pathway to Decarbonisation which was approved by our Board in March 2021.

The feedback from our engagement and research programme is helping shape the Group's Environmental, Social, Governance strategy.

This year, in response to stakeholder feedback about improved governance, we have set up an Environment Advisory Panel to challenge and provide support with our sustainability strategy and action plan. The panel of industry sustainability experts will provide insight into the current and future needs of our stakeholders, customers and communities and suggest appropriate actions to improve our environmental performance.

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S172(1) (E) "The desirability of the company maintaining a reputation for high standards of business conduct"

The Directors' aim to ensure that the Company maintains high standards of business conduct through the support of the Company's culture and values which underpin decision making at a Board and management level.

- **Safety first** - We take responsibility for our own safety and the safety of those around us
- **Driving performance** - Efficiency, innovation and continuous improvement will help us deliver excellence and achieve commercial success
- **Putting people at the heart** - we always work together, talk honestly and trust people with respect
- **Looking after customers** - by listening to our customers, understanding their needs and keeping our promises we can deliver an excellent service that people trust
- **Sustaining our world** - we maximise our effect on local communities and minimise our impact on the world

S172(1) (F) "The need to act fairly as between members of the company"

The Directors' recognise the responsibility to act fairly as between members of the company. This is outlined by the Company's vision, purpose, and engagement which is supported by the Board of Directors.

- **Our vision** is to own heat and lead the way in low carbon energy delivery by making gas green
- **Our purpose** is to keep everyone safe and warm; and strategy is to deliver long-term value for existing and future customers, stakeholders and shareholders. A strategy based on strong financial management and governance framework.
- **Our engagement** we engage with our employees and wider stakeholders in the right way to help foster relationships and deliver long term value for existing and future customers, employees and stakeholders.

The Directors' Report outlines further examples of how each of the sub-committees of the Board have applied these principles in key decision-making activities.

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ENGAGEMENT WITH EMPLOYEES

We will only deliver our vision if we recruit, skill and retain the best talent and develop a flexible, motivated, efficient, diverse and engaged team.

The Board has adopted a robust employee listening strategy, capturing feedback, insight and suggestions from colleagues using a range of different methods and channels. The feedback is subject to rigorous analysis to identify emerging themes and trends.

We have ongoing, two-way channels for engaging with our people. This ranges from, on site and office visits, Lets Chat sessions, regular communication via internal channels and media platforms, employee forums and structured engagement with trades unions and pension trustees.

Employee pulse surveys help measure progress made with our engagement plans and make sure we're moving in the right direction. Our diversity & inclusion networks help us promote a diverse and inclusive culture through events and awareness campaigns. They include: Insight Action Group, D&I Partners, Let's Talk about Race, Rise Programme, and Future Thinkers Panel. Our learning management system ensures we can deliver training and development to make SGN a success. We monitor safety through KPI reporting and take action to continuously improve the safety of our working environment. We have regular team updates, and briefings, via our Extended Leadership Team town hall sessions, Team Talk, our App and Digital HUB intranet portal which includes a CEO and Executive blogs and other communications including podcasts and listening sessions, which employees can listen at their convenience.

A report from the HR & Services Director is submitted to each board meeting and the results of employee engagement surveys are also presented at board meetings.

Engagement with our people ensures that employees remain informed about business strategy and developments in real-time.

Corresponding feedback allows both management and the Board to ensure areas of importance highlighted by employees' perspectives are considered and reflected in future decisions and communications. The employee engagement survey results are reviewed at management, executive and Board level. Each business area uses the feedback to develop action plans and inform its approach, which is communicated to employees and teams. This feedback has directly informed the Board's decision making to approve two new offices in Glasgow and Horley and for these to embrace modern ways of working.

Key board decisions made in the year that impact our employees:

- New offices in Glasgow and Horley
- Safe to Speak up Campaign

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ENGAGEMENT WITH SUPPLIERS, CUSTOMERS AND OTHERS

We are a business which truly listens to our stakeholders, taking steps to ensure everyone has an opportunity to share with us their views about what matters to them. We've used the valuable insight gathered from our customers and stakeholders to shape our business, and now structure our activities to align with the customer and stakeholder-driven commitments:

- We will make a **positive impact** on society, by supporting vulnerable communities and providing excellent service.
- We will deliver a **safe and efficient** service by acting safely, keeping the gas flowing and keeping costs down.
- We will build a **shared future** by accelerating decarbonised energy solutions and minimising our environmental impact.
- We will **create value** by accelerating commercial opportunities which complement the core; maximise the value from our existing asset base; invest in opportunities for the sustainability of our network and keep the Company at the forefront of the delivery of heat.

As outlined in the s.172 statement, in response to stakeholder feedback about improved governance, we have set up an Environment Advisory Panel to challenge and provide support with our sustainability strategy and action plan. The panel of industry sustainability experts will provide insight into the current and future needs of our stakeholders, customers and communities and suggest appropriate actions to improve our environmental performance.

Continuous Improvement

We strive for continuous improvement in our approach to stakeholder engagement. Our longstanding six principles guide our approach to stakeholder engagement and are detailed below.

1. Delivering measurable benefits:

We will engage directly with customers and stakeholders to embed their interests in our decision-making and deliver valued, measurable benefits.

2. Focusing on material issues:

Customers and stakeholders should have a say in relevant issues they care about and that will have the most impact on them, both now and in the future.

3. Driving inclusivity and diversity:

Engagement with customers and stakeholders should be broad and inclusive; we will seek out the diverse perspectives of challenging and hard to reach groups and ensure complex issues are communicated in a way that is easily accessible and understandable to all.

4. Providing ongoing opportunities for challenge and collaboration:

Engagement will be tailored to the needs of stakeholders to ensure genuine opportunities for ongoing dialogue, mutual education, challenge, review and collaboration are created.

5. Being responsive and transparent:

The Company will be responsive and transparent, explaining how the views and priorities of stakeholders have influenced decision-making and how we have balanced the needs of different stakeholders.

6. Continually improving:

The Company will continuously improve and develop its engagement with customers and stakeholders, finding new and more innovative approaches to respond to their changing needs.

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for the Year Ended 31 March 2021**Our six-stage engagement cycle**

Our engagement strategy details the six, iterative stages of our engagement cycle we use to embed the above principles of stakeholder engagement across our organisation. These are as follows:

1. For each of our key businesses priorities and processes we identify the stakeholders impacted by or interested in our activities
2. We tailor our methods of engagement with our stakeholders depending on their preferences and their levels of knowledge and interest
3. We engage with a purpose and listen to our stakeholders
4. We respond to the views of stakeholders across our business
5. We measure the benefits of our engagement and its effectiveness
6. We review and refine our strategy and engagement plans

Identifying and mapping our key stakeholders

Our digital Stakeholder Relationship Management (SRM) tool allows us to capture and analyse our engagement activities with a diverse range of stakeholders across our business. We use SRM to maintain records of which topics each stakeholder has told us are priorities or of interest to them, the geographical areas in which they operate and their communication preferences.

Our stakeholders are categorised into one of twelve main groups as outlined below.

Supporting Section 172

A critical aspect of working constructively with the Company's key stakeholder groups is the engagement which takes place to understand material issues of interest and set out below are details of the engagement mechanisms that exist within the Group, which ultimately support the Board's understanding of relevant stakeholder views. This approach ensures that all decision-making is adequately informed and is supportive of a Director's duty under Section 172 of the Companies Act 2006.

The Board had regard to the interests of all stakeholder groups were considered during the shaping of the 5-year business plan

Stakeholder type	Key stakeholders	2020/21 Board impact areas
Internal Stakeholders SGN employs around 4,000 people across its workforce and has four shareholders.	Employees/workforce, trade unions, shareholders	Employee engagement and action plan, remuneration, talent and succession, diversity and inclusion. New offices in Glasgow and Horley and introduction of the Safe to Speak up Campaign
Customers SGN provides gas distribution and related services to millions of customers.	Domestic and industrial customers, small and medium enterprises, future of gas customers	Sustainability - pathway to the decarbonisation of heat, environmental action plan, safety performance, Customer GD2 strategy, Business Plan. New vulnerability strategy developed and ready for implementation throughout 2021/22.

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Regulatory bodies SGN works constructively with regulatory bodies	Ofgem, HSE, Environment Agency, SEPA	Stakeholder engagement strategy, sustainability - pathway to the decarbonisation of heat, environmental action plan, safety performance. Decision to refer certain elements of the RIIO-GD2 Process to the CMA. Approval or acknowledgment of Ofgem Statutory Licence Consultation
Local government SGN works constructively with central and local government	Government departments, local authorities, politicians, local energy plan partners	Stakeholder engagement strategy, sustainability - pathway to the decarbonisation of heat, environmental action plan, UN sustainability development goals
Energy partners and industry peers SGN works in collaboration with third party energy partner providers and industry peers	GDNs/DNOs, shippers/suppliers, industry groups, IGTs/UIPs, other utilities (water, telecom, etc.)	Sustainability - pathway to the decarbonisation of heat, environmental action plan, UN sustainable development goals
Supply Chain SGN works closely with its supply chain	Appliance manufacturers, construction and engineering companies, services providers	GD2 Contracts, Living Wage, Supply Chain Sustainability School
Local interests SGN works in partnership with many third-party organisations to support local interest	Community groups, energy and health services, public transport providers, housing providers	Sustainability - pathway to the decarbonisation of heat, environmental action plan, UN sustainable development goals
Environmental experts and Advisory groups SGN works closely with its environmental groups to ensure it minimises its environmental impact	NGOs, environmental charities, sustainability specialists	Sustainability - pathway to the decarbonisation of heat, environmental action plan, UN sustainability development goals
Consumer welfare agency groups/providers SGN works closely with its consumer welfare groups to support vulnerable communities	Consumer groups, charities, private and community interest groups	Sustainability - pathway to the decarbonisation of heat, environmental action plan, UN sustainability development goals. New vulnerability strategy developed and ready for implementation throughout 2021/22.

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for the Year Ended 31 March 2021**Key performance indicators**

The Company measures the achievement of its objectives through the use of quantitative assessments and, where quantitative measures are less relevant, through the use of qualitative assessments. The principal key performance indicators ("KPIs") which are used to assess whether principal operating objectives have been achieved are set out below:

Key performance indicator	Description	Year ended 31 March 2021	Year ended 31 March 2020
Revenue	Income relating to the transportation of natural gas and provision of related services	£806m	£817m
Operating profit	Profit before financing costs and taxation	£345m	£373m
Capital expenditure [5]	Additions to fixed assets	£76m	£92m
Replacement expenditure [5]	Replacement expenditure is capitalised under FRS 102. It represents the cost of renewing sections of gas network with polyethylene pipes.	£189m	£224m
Net Debt to RAV ratio [1]	The Company's debt to RAV ratio	70.1%	71.6%
Employee lost time incidents	Incidents resulting in employees taking time off work (per 100,000 hours worked)	0.06 [4]	0.08 [4]
Customer satisfaction - planned interruptions	Results from customer satisfaction surveys (10 = very satisfied)	9.0 [2]	8.8 [2]
Customer satisfaction - unplanned interruptions	Results from customer satisfaction surveys (10 = very satisfied)	9.6 [3]	9.4 [3]
Escapes attendance	Proportion of uncontrolled escapes attended in one hour - percentage (target 97%)	98.9%	98.5%
Customer complaint volume reduction/increase	This represents the year on year reduction in complaints expressed as a percentage. Complaint means any expression of dissatisfaction related to any areas of our operation.	39% decrease [4]	20% increase [4]

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Strategic Report
for the Year Ended 31 March 2021

- [1] "RAV" is defined as Ofgem Regulatory Asset Value plus adjustments relating to the sharing of out/under performance against allowances. Net debt for the purposes of the Debt to RAV ratio includes unrestricted cash, short term deposits and intercompany loans but excludes liabilities arising from derivative financial instruments. The percentages stated are as at 31 March.
- [2] Based on customer satisfaction survey reports obtained for the nine-month period ended 31 December 2020 and 2019 for the Group.
- [3] Based on customer satisfaction survey reports obtained for the nine-month period ended 31 December 2020 and 2019 for the Group.
- [4] This KPI is measured for the Group, and accordingly the data presented is that for the Group.
- [5] The sum of capital expenditure and replacement expenditure equal the total additions of intangible and tangible fixed assets as reported in notes 10 and 11 respectively.

Resources

The Company's principal resources are its assets and its people.

The Company's distribution network comprises approximately 49,000 kilometres of gas mains, together with associated services, plant and machinery and storage facilities.

The Company had 470 full time equivalent employees at 31 March 2021 (2020: 506). It places considerable value on the involvement of employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Company during the year. It continues to invest in the development and training of its people in order to ensure both individual developmental needs and business skill requirements are met.

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Strategic Report
for the Year Ended 31 March 2021

FINANCIAL REVIEW

The Company sets out below its financial review for the year ended 31 March 2021. The comparative figures presented are for the year ended 31 March 2020, as reported in the audited financial statements, unless otherwise stated.

Turnover for the year ended 31 March 2021 was £806m (2020: £818m). There was an inflationary increase in turnover, the impact of which was mitigated by a high level of revenue being shared with customers, which remains a substantial deduction from revenue due to SGN's outperformance of the allowances set by Ofgem. The majority of turnover was earned from charges made for the provision of gas transportation capacity as well as revenue based upon gas volumes transported in the year.

Profit for the year before taxation amounted to £243m (2020: £259m) and profit for the year after taxation amounted to £196m (2020: £148m). The current year tax charge is significantly lower than the tax charge in the year ended 31 March 2020. This is mainly due to a change in the tax rate in the prior year which resulted in a £61m increase in the company's deferred tax liability in the year ended 31 March 2020. No such rate change occurred in the financial year ended 31 March 2021.

Operating profit decreased to £345m (2020: £373m) driven by the above-mentioned decrease in turnover and an increase in operating costs.

The Company paid dividends of £81m (2020: £53m) during the year.

Capital expenditure (excluding replacement expenditure) during the year amounted to £76m (2020: £92m). Capital expenditure is incurred to ensure that the networks continue to operate at minimum agreed pressures and that sufficient storage capacity is available to meet instances of peak demand, as well as when new connections or increased capacity are added to the networks. There was a decrease in capital expenditure in the year which was attributable to a reduction in workload at the start of the year due to national restrictions imposed by the UK Government in response to the global Covid-19 pandemic.

Treasury policies and capital structure

The Company's operations are financed by a combination of equity and retained profits, bank borrowings and long-term bonds. The Company's funding and liquidity are managed within a framework of policies and guidelines authorised by the Board of Directors. Further details are set out in the Directors' Report.

As a matter of policy, a minimum of 75% of debt is maintained at either fixed rates of interest or index linked. This policy is kept under review from time to time. Interest rate swaps are used, where necessary, in order to achieve this desired profile.

As at 31 March 2021, the Company's total senior debt (before issue costs) amounted to £2,960m (2020: £2,921m) and the debt to RAV ratio was 70.1% (2020: 71.6%). Of the total long-term borrowings at 31 March 2021, after taking into account the effect of interest rate swaps, 89.8% were at either fixed rates of interest or were index linked (2020: 89.7%).

Southern Gas Networks Plc (Registered number: 05167021)Strategic Report
for the Year Ended 31 March 2021**Pension commitments**

A large proportion of the Company's employees are members of the Scotia Gas Networks Pension Scheme which provides final salary defined benefits for members.

The Company accounts for any pension asset or liability in accordance with FRS 102. The net pension asset as at 31 March 2021 was £179m (2020: £213m). Annual special pension contributions decreased for the Group in the year ended 31 March 2021 totalling £12.5m (Company's share: £7.5m). These additional contributions will be paid annually until 31 March 2027 to repair the actuarial deficit in the defined benefit pension scheme. The Company's normal contributions remain at 37.3%. The Company's actuary undertook a triennial review during 2018/19 to update the actuarial deficit for recent changes in external and market conditions.

Liquidity risk

Liquidity is maintained through a mixture of long term borrowings and short-term liquid funds in order that there are sufficient funds available for the Company's current and planned operations. Committed facilities are in place in order to provide funding for future capital and replacement expenditure as well as to provide sufficient available facilities to meet the seasonal working capital requirements of the Company. The revolving credit facility totalled £360m for the Group (2020: £360m) and is in place until March 2025; as at 31 March 2021 £360m is undrawn (2020: £360m). At 31 March 2021 the Company's committed undrawn revolving credit facility amounted to £240m (2020: £340m).

Counterparty credit risk

The Company transacts with banks for the provision of interest rate and currency hedging transactions. The Company takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy; however, it recognises that at times the market conditions for banks can be unusually tight. At the year end the Company had £21m payable relating to financial instruments with bank counterparties (2020: £26m).

Dividend policy

The Company's policy is to manage the level of distributions after taking into consideration the expected cash flows and investment plans across the business, the level of committed funding available as well as the gearing covenants and targets set by the Board.

Accounting policies

The Company's accounting policies are set out in note 1 to the financial statements. These accounting policies have been applied consistently during the year and in the preceding year.

OPERATIONAL REVIEW**Safety****Injury performance**

The Company's overriding goal is to distribute gas safely and reliably and to ensure a safe workplace for its workforce with everyone striving towards eliminating injuries. This year the lost time injury performance rate decreased to 0.06 injuries per 100,000 hours (2020: 0.08).

Board responsibility

The Board has a Safety, Health and Environmental Advisory Committee that is responsible for monitoring health and safety performance and ensuring the health and safety policy statement is adhered to. The Committee provides the Board with reports on any key areas identified and further details on the Committee are set out in the Corporate Governance Statement, in the Directors' Report.

Southern Gas Networks Plc (Registered number: 05167021)

Strategic Report
for the Year Ended 31 March 2021

Gas mains replacement programme

The Company replaces the iron pipes with modern polyethylene pipes to improve the safety of the existing network. Replacement expenditure, primarily of iron pipes, reduced to £189m (2020: £224m). In line with movement in capital expenditure, there was also a decrease in replacement expenditure in the year which was due to a reduction in workload at the start of the year due to national restrictions imposed by the UK Government in response to the global Covid-19 pandemic.

Gas escapes standards of service

The Company's engineers respond to reports of suspected gas leaks 24 hours a day, 365 days a year, regardless of from whom people buy their gas. Its engineers aim to attend all uncontrolled gas escapes within one hour and all controlled gas escapes within two hours. A controlled gas escape is one where the person reporting it has confirmed that the gas emergency control valve serving the premises has been turned off and the smell of gas has gone. An uncontrolled gas escape covers all others. The Company's engineers exceeded Ofgem targets by attending over 99% (2020: 98%) of uncontrolled gas escapes within one hour.

Gas networks' regulation

Gas network companies are subject to economic regulation through Price Control Reviews set by industry regulator Ofgem. The current eight-year price control (RIIO) commenced in April 2013 and completed on 31 March 2021.

Revenues are earned through charges levied on network users, to cover costs and earn a return on the network company's regulated assets. Ofgem also has incentives in the price control to encourage greater efficiency, innovation and delivery of an enhanced standard of service for customers.

With eight years of RIIO complete the Company has performed well on outputs set by the regulator, including those for innovation, customer satisfaction and stakeholder engagement. Ofgem published the final determination for RIIO-GD2 which will place significant challenges on the business regarding the need to deliver considerable efficiencies due to tight regulatory allowances. During the year a number of initiatives have been planned across the business and will be implemented in the coming years to ensure the Company is in the best position to cope with the new demands.

Further details

Further details on the long-term development plans of the Company can be found in the long-term development statement (published in accordance with Special Condition D3 of the Gas Transporter Licences) and available on the Company's website - www.sgn.co.uk. The long-term development plans set out the forecast gas demand over the ten-year period and outlines the capital investment plan that is required to ensure the continued operation of the network in accordance with the Company's licence conditions.

APPROVED BY THE BOARD AND SIGNED ON ITS BEHALF BY:

DocuSigned by:

Nick Salmon

8044CB5BCFE1453

Nicholas Robin Salmon (Chair) - Director

Date: 20 July 2021

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

The Directors present their report and the audited financial statements for the year ended 31 March 2021.

PRINCIPAL ACTIVITY

The Company's principal activity is the development, administration, maintenance and operation of the South and South East of England gas distribution system and the supply of gas transportation services. It will continue in this activity for the foreseeable future.

DIVIDENDS

The Company paid an interim dividend of £81m (2020: £53m). The Directors do not recommend the payment of any final dividend for the year (2020: £nil).

FUTURE DEVELOPMENTS

Details of future developments can be found in the strategic report.

EVENTS SINCE THE END OF THE YEAR

Information relating to events since the end of the year is given in the notes to the financial statements.

DIRECTORS

The directors shown below have held office during the whole of the period from 1 April 2020 to the date of this report.

Gregor Alexander
Charlotte Brunning
Paul Jeffery
Guy Lambert
Robert McDonald
Charles Thomazi (Alternate)
Nicholas Robin Salmon (Chair)
Laura Sandys
Peter Mccosker (Alternate)
Michael McNicholas

Other changes in directors holding office are as follows:

Natalie Flageul - resigned 22 July 2020
John McManus - resigned 1 July 2020
Ines Grund (Alternate) - resigned 3 November 2020
Delphine Voeltzel - appointed 1 July 2020

DIRECTORS' INSURANCE AND INDEMNITIES

The Directors of the Company have the benefit of the indemnity provisions in the Company's Articles of Association. The Directors have been granted a qualifying third-party indemnity provision which was in force throughout the year. In addition, SGN has purchased and maintained throughout the year Directors' and officers' liability insurance in respect of itself, the Group, the Directors and other senior executives of the Group.

REVIEW OF BUSINESS

The review of business for the year, including an analysis using key performance indicators, together with a description of the principal risks and uncertainties facing the Company are set out in the strategic report.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

FINANCIAL RISK MANAGEMENT

The Company's funding, liquidity and exposure to interest rate and foreign exchange risks are managed within a framework of policies and guidelines authorised by the Board of Directors.

Interest rate risk

The Company has interest bearing liabilities, and as a matter of policy a minimum of 75% of debt is maintained at either fixed rates of interest or index linked. This policy is kept under review from time to time. The Company uses interest rate swaps, where necessary, in order to achieve this desired profile.

Foreign exchange risk

All of the Company's borrowings are currently denominated in Pound Sterling, so there is no foreign exchange risk. However, in accordance with its policy, should the Group decide to raise finance in currency other than Pound Sterling, cross currency swaps would be used to fully hedge the borrowings into Pound Sterling.

Liquidity risk

The Company maintains a mixture of long-term funding and short-term liquid funds in order to ensure that there are sufficient funds available for the Company's current and planned operations.

Credit risk

The Company transacts with banks for the provision of interest rate and currency hedging transactions. The Company takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy; however, it recognises that at times the market conditions for banks can be unusually tight. In respect of short-term cash management, counterparties are subject to review and approval according to defined criteria.

Trade receivables predominantly relate to transportation income from gas shippers. Credit risk arising from the Group's regulated business is managed in accordance with industry standards as set out by the Unified Network Code. Credit risk on amounts receivable from other Group companies is considered minimal.

Pricing risk

The Company's gas transportation charges are subject to price control formulae set within the regulatory regime. The Company's maximum allowed revenue in a given price period is dependent upon a number of factors that are not known in advance and therefore the maximum allowed annual revenue is not known until the end of the relevant period.

However, transportation tariffs are set on a prospective basis based upon expected transportation volumes, so actual revenue received or receivable in any one year may differ from the maximum allowed revenue. Where revenues received or receivable differ from the maximum allowed annual revenue, adjustments are made to future prices to reflect this over or under recovery.

EMPLOYEES

The Company places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the Company. Participation by employees generally is encouraged through team meetings, briefings, a digital app and an intranet site. The CEO and other senior executives regularly communicate with employees through these channels and employee representatives are consulted regularly on a wide range of matters affecting their current and future interests.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure their employment within the Company continues and that appropriate training and development is arranged. It is the policy of the Company that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

GOING CONCERN

The Company's accounts have been prepared on a going concern basis.

The directors have forecast cash flows of the company for the next twelve months (the going concern period) and have obtained a support letter from Scotia Gas Networks Limited confirming that it can and will support the Company in meeting its liabilities throughout the going concern period.

In assessing the ability of the company to rely on this support the directors have considered the impact of COVID-19 on the Group and the going concern assessment undertaken at the Scotia Gas Networks Limited group level, the conclusion of which is that even under severe but plausible downside scenarios there is headroom in relation to both liquidity and covenants.

Consequently, the directors believe that the Company will be able to meet its liabilities as they fall due and will have adequate resources to continue in operational existence for 12 months from the date of approval of this report. Accordingly, the directors continue to adopt the going concern basis in preparing the financial statements.

ENVIRONMENT AND SUSTAINABILITY

This year, in response to stakeholder feedback about improved governance, we have set up an Environment Advisory Panel to challenge and provide support with our sustainability strategy and action plan. The panel of industry sustainability experts will provide insight into the current and future needs of our stakeholders, customers and communities and suggest appropriate actions to improve our environmental performance. The panel is chaired by Kathryn Dapr , Head of Energy and Sustainability at NHS National Services Scotland, and includes members from our CEG and Stakeholder Advisory Panels.

Progress on targets

We are currently working with a "keep up the good work" approach, monitoring and reporting our carbon footprint, waste and the impact the business has on the environment.

Natural gas shrinkage is made up of leakage of natural gas (which contains the greenhouse gas methane) from the network, own use of gas and theft of gas. This is the biggest part of the Group's carbon footprint accounting for 96.8% (2020: 95.6%). Reducing shrinkage therefore has the largest effect on reducing our carbon footprint. Over the year the Group have achieved a 3.2% reduction in natural gas shrinkage (2020: 4.0%) which equates to 24,458 tonnes of CO₂ equivalent (2020: 31,492). The reductions are largely achieved through our iron mains replacement programme, optimising and driving down operating pressures in the network, gas conditioning and investment and innovation.

This year Covid-19 has impacted our operations which will have restricted our ability to reduce our TCF in line with our aims at the start of the year. This is largely due to the work that had to be stopped on our iron mains replacement programme as it was deemed non-essential operations. Replacing the old iron mains with new polyethylene (PE) pipes dramatically reduces methane leakage, our largest area of CO₂ emissions. Our CO₂e reduction targets were based on fulfilling our planned replacement programme, so by not doing delivering our replacement targets our CO₂e reduction targets will not have been met.

Southern Gas Networks Plc (Registered number: 05167021)Directors' Report
for the Year Ended 31 March 2021

However, our BCF reduction efforts will have benefited by less emissions from our commercial fleet, thanks to stopped non-essential work. We also expect to see reduced CO₂e from less electricity consumption due to employees working from home. Scope 3 emissions (indirect emissions) have also been reduced, thanks to around 60% less business travel than the previous year (air, train, car and company car), less embodied carbon in PE pipe (as we have used less PE pipe), and less contractors' carbon (e.g. their lower fleet emissions).

In 2020 we changed our waste management provider to reduce waste going to incineration (which is harmful to air quality). Our waste to landfill rates have hence gone up to 3% from zero. We are working with our current waste management provider to reduce waste to landfill through re-use and recycle.

Spoil to landfill is continuing to reduce and we are aiming for zero non-hazardous waste to landfill by 2026. This will also include waste from our depots and offices, and we are working with our waste management provider to reduce landfill waste through re-use and recycle. By 2026 we are aiming to use no more than 0.1% virgin material for reinstatement works in our Southern network and no more than 20% virgin material for our Scottish network. Scotland has one of the lowest numbers of recycling centres of all gas distribution areas due to its geography and low population density, reducing SGN's access to recycled material.

The overall Carbon Footprint (compliant with Streamlined Energy and Carbon Reporting, SECR) for the Company is shown in the Table below:

	2020/21		2019/20		Annual Movement Decrease/ (increase)	
	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover
Scope 1						
Energy consumption (excluding electricity)	273	0.34	182	0.22	(91)	(0.12)
Transport (direct commercial vehicles and business miles)	7,410	9.18	7,727	9.45	317	0.27
Scope 2						
Electricity consumption	94	0.12	2,123	2.60	2,029	2.48
Scope 3						
Rail, air and ferry travel	7,648	9.48	13,229	16.18	5,581	6.70
Total (excluding shrinkage)	15,425	19.12	23,261	28.45	7,836	9.33
Shrinkage	542,816	672.63	562,275	687.60	19,459	14.97
Total carbon emissions	558,241	691.75	585,536	716.05	27,295	24.30

Data has not been independently verified

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Directors' Report
for the Year Ended 31 March 2021

STATEMENT OF CORPORATE GOVERNANCE ARRANGEMENTS

The Board has considered the Companies (Miscellaneous Reporting) Regulations 2018 (the 'Regulations'). Companies that meet certain thresholds are required to report under four corporate governance reporting regimes:

1. Stakeholder Engagement - A statement on how directors have engaged with stakeholders and how directors have had regard to stakeholder interests.
2. Corporate Governance - A statement on the Company's Corporate Governance Arrangements and how these have been applied.
3. Employee Engagement - A statement on how directors have engaged with employees and how directors have had regard to employee interests.
4. Section 172 - A statement on how Directors have had regard to their Section 172 duty to promote the success of the Company, as set out in the Companies Act 2006.

The Company has adopted all four of these reporting regimes (Corporate Governance Requirements). In readiness, the Company has established a governance programme to ensure Directors are able to comply with these Corporate Governance Requirements.

Internal controls in relation to the Group's financial reporting process

The Board of Directors is ultimately responsible for the Company's internal control systems and risk management. The Company's system of internal control and embedded risk management, which have been in place throughout the year, help to safeguard the assets and are designed to manage, rather than eliminate, material risks to the achievement of the business objectives. The Board recognises that these systems can provide only reasonable, and not absolute, assurance against material misstatement or loss.

Accordingly, the Directors have regard to what controls, in their judgement, are appropriate to the business, to the materiality of the risks inherent in the business and to relative costs and benefits of implementing specific controls. Internal control is maintained through an organisation 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 periodic review as to their implementation and continued suitability. There were no changes in the Company's internal controls over financial reporting during the year covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Internal audit

The Board of Directors has established the scope of the internal audit function which is responsible for reviewing the effectiveness of the Company's systems of internal control and reports to the Audit Committee of the Board. The internal audit manager reports to the Audit Committee on the audit programme, progress against the programme and any follow-up actions on a bi-monthly basis.

Wates Principles

1. Purpose and leadership

An effective Board develops and promotes the purpose of a company, and ensures that its values, strategy and culture align with that purpose.

2. Board composition

Effective Board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual directors having sufficient capacity to make a valuable contribution. The size of a Board should be guided by the scale and complexity of the company.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

3. Director responsibilities

The Board and individual directors should have a clear understanding of their accountability and responsibilities. The Board's policies and procedures should support effective decision-making and independent challenge.

4. Opportunity and risk

A Board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value, establishing oversight for the identification and mitigation of risks.

5. Remuneration

A Board should promote executive remuneration structures aligned to the long-term sustainable success of a company, considering pay and conditions elsewhere in the company.

6. Stakeholder relationships and engagement

Directors should foster effective stakeholder relationships aligned to the company's purpose. The Board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions.

Corporate Governance

During the year ended 31 March 2021, the Company has applied the Wates Corporate Governance Principles for Large Private Companies (Wates Principles) as part of its wider Corporate Governance Requirements. The Wates Principles are published by the Financial Reporting Council ('FRC') and available on the FRC website. In this Directors' Report, we describe how we have applied the Wates Principles in line with its 'comply or explain' model and confirm full compliance with its principles for the reporting year ended 31 March 2021.

Principle 1 - Purpose and leadership

An effective Board develops and promotes the purpose of a company, and ensures that its values, strategy and culture align with that purpose.

Our vision is to own heat and lead the way in low carbon energy delivery by making gas green. Our purpose is to keep everyone safe and warm and our strategy is to deliver long-term value for our existing and future customers, stakeholders and shareholders.

The Board is responsible for ensuring that values, strategy and culture are aligned with our vision and purpose. Our Strategic Pillars embed our vision, purpose and values as key elements to ensure our stakeholders' interests are central to our long-term success.

During the financial year we worked with our people and stakeholders to ensure we are fit for our future and focussed on delivering our business plan as we prepared to move from RIIO-GD1 to RIIO-GD2. Looking ahead to FY21/22, we are planning a culture audit to see how we are performing against our core value to put people at the heart of what we do by creating an inclusive workplace for all.

Principle 2 - Board composition

Effective Board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual directors having sufficient capacity to make a valuable contribution. The size of a Board should be guided by the scale and complexity of the company.

The Board comprises eight Non-Executive Directors, including a separate Chair to the Chief Executive, to ensure that the balance of responsibilities, accountabilities and decision making across the Company are effectively maintained. The Chief Executive, Chief Financial Officer and the Director of Legal Services & Group Company Secretary attend each Board meeting. Two Independent Non-Executive Directors also sit on the Company Board.

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Directors' Report
for the Year Ended 31 March 2021

The Independent Non-Executive Directors bring outside experience in utilities, energy policy and finance, and provide constructive challenge and influence. The composition of the Board is partly determined by the Shareholders' Agreement and it is considered to be in the best interests of the Company for the CEO, CFO and each Shareholder to be represented at meetings. We consider that there is an appropriate combination of skills, backgrounds, experience and knowledge that promotes accountability.

Towards the end of financial year, Gregor Alexander stepped down as Chair following 10 years and Nick Salmon was appointed as Chair. Gregor Alexander remains on the Board and in advance of this rotation supported with the succession and transition to Nick Salmon.

As part of his new role as Chair, Nick Salmon has completed one-to-ones with each Director, which was followed by a short board evaluation and report from the Director of Legal Services & Group Company Secretary. From this feedback, we have planned a Board strategy day for FY21/22 and are also planning a culture audit to see how we are performing against our core value to put people at the heart of what we do by creating an inclusive workplace for all. The Board is also committed to improving its diversity in terms of gender, ethnicity, disability and age, and its People and Reward Committee is responsible for reviewing diversity and succession planning.

Principle 3 - Director responsibilities

The Board and individual directors should have a clear understanding of their accountability and responsibilities. The Board's policies and procedures should support effective decision-making and independent challenge.

The SGN Group has a separate Chair and CEO to ensure that the balance of responsibilities, accountabilities and decision making are effectively maintained. The Board receives regular reports on financial and operational performance, customers, people and stakeholders and management of key business risks along with updates on activities and decisions of its committees. Independent Non-Executive Directors provide constructive challenge to the Board's decision-making process.

The Board continue to be supported by the work of the Board Committees. During the year, a review and update to the Committee Terms of Reference and Board Responsibilities was completed to ensure clear understanding of accountability and responsibilities. In FY21/22, a review of the Board Reserved Matters is planned to ensure the balance of responsibilities, accountabilities and decision making is maintained between the Executive Committee, Board and new subsidiary companies within the group, as the Group continues to grow and diversify.

Principle 4 - Opportunity and risk

A Board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value, establishing oversight for the identification and mitigation of risks.

The SGN Board seeks out opportunity while mitigating risk. Long-term strategic opportunities and high value investments are presented to the Board. The Executive Committee ensure that inherent and emerging risks are identified and managed appropriately and in a timely manner updating the risk register for any changes in underlying conditions and reporting this through to the Board. Operational and safety risks are regularly reviewed by the Risk Committee and financial risks by the Audit Committee.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

The Board formally reviewed the key strategic risks both at the half and full year point, which now encompasses a formal review of emerging risks taking insights from an independent consultant to help shape this discussion. The Board plan to review the risk appetite and target risks in FY21/22 to ensure these reflect the RII0-GD2 plan and pathway to decarbonisation. The Board also review key investment opportunities throughout the year. A Board priority setting exercise is also planned for the AGM to forward plan the Board programme ensuring a balance of steering and supervisory items to help review, amongst other things, opportunities and risk to preserve value for the long-term sustainable success of the Company.

Principle 5 - Remuneration

A Board should promote executive remuneration structures aligned to the long-term sustainable success of a company, considering pay and conditions elsewhere in the company.

The People and Reward Committee has clearly defined terms of reference and is responsible for making recommendations to the Board concerning the Company's remuneration strategy, recruitment framework and long-term incentive plans for senior executives. The Committee takes advice from independent external consultants who provide updates on legislative requirements, best market practice and remuneration benchmarking. The primary objective is to set remuneration at a level that will enhance the Company's resources by securing and retaining quality people who can deliver our Strategic Pillars and long-term value for its existing and future customers, stakeholder and shareholders.

In FY20/21, the Board (following a recommendation from PARCO) agreed changes to the both the short term and long-term incentive plan to align these against the Strategic Pillars to ensure a better alignment to support delivering what matters to stakeholders including our pathway to decarbonisation. A review of the Executive remuneration policy was also completed in the year which included a move to 80:20 company and personal performance split of short-term incentives. We propose to review the short-term incentive framework again in FY21/22 which will provide an opportunity to reflect any changes flowing out of the Board strategy day.

Principle 6 - Stakeholder relationships and engagement

Directors should foster effective stakeholder relationships aligned to the company's purpose. The Board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions.

The Board is aware of the broader impact it has on its various environments, its customers and society in general, and has established corporate social responsibility policies and practices for the Company. The Board is committed to social responsibility, community engagement and environmental sustainability as underpinned by our Strategic Pillars.

Covid-19 has shown that stakeholder engagement and our corresponding responses to events must be dynamic. The focus and priority during the Year, have been to focus on our core purpose to keep everyone safe and warm. Regular two-way engagement with our stakeholders has been central to this and helping us shape decision.

In June 2020, our newly established Stakeholder, Environment and Customer Committee (SECC) met for the first time and continued to meet during the year. Listening to feedback and committed to making gas green, we have developed our ESG strategy which we will continue to build and improve. We also plan to continue to build on our engagement by agreeing a formal, but dynamic, board stakeholder engagement plan to ensure we continue to foster relationships and build at putting stakeholder views at the end of what we do.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

Board of Directors

The Board of Directors is comprised entirely of Non-Executive Directors and is the principal decision-making forum for the Company. Directors are nominated to the Board in accordance with the terms of the Shareholders' and Governance Agreement.

The Board is collectively responsible for the long-term success of the Company and for setting of a clear purpose, vision and sustainable strategy which creates value for existing and future customers, stakeholders and shareholders. It provides the leadership necessary for the Company to meet its business objectives while ensuring a sound system of internal control and risk management is in place. The powers and the duties of the Directors are determined by legislation and by the Company's Articles of Association. The Board has also adopted a formal schedule of matters detailing key aspects of the Company's affairs reserved to it for decision.

The Board of Directors comprises nine Non-Executive Directors. This consists of a Non-Executive Chair and eight Non-Executive Directors.

The Non-Executive Directors scrutinise, measure and review the performance of management; constructively challenge and assist in the development of strategy; review the Company financial information; and ensure systems of internal control and risk management are appropriate and effective.

Chair

On 1 March 2021, Nick Salmon was appointed Chair, following rotation from Gregor Alexander who remains in the Board.

Board Committees

During the year the Board was directly assisted in the discharge of its duties by five Board Committees and dedicated GD2 Board meetings, whose remit, authority and composition are monitored to ensure continued and appropriate Board support.

Each of the Board Committees provides dedicated focus to a defined area of responsibility. Board Committees act as an advisory body, with the Board retaining oversight and final decision making, except where otherwise delegated by the Board in which case the Committee will act within their agreed authority.

Board Committee membership is determined by the Board. Prior to determining membership, the Board will consider the subject matter of the Committee's purpose and duties to ensure that the membership addresses its specific needs. Membership will assess technical skills, knowledge and experience whilst recognising the benefits associated with diversity. Each Board Committee is chaired by a Non- Executive Director.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Board effectiveness

The Group Company Secretary, Chief Executive Officer and newly appointed Chair conducted a governance review and gathered Board feedback on its effectiveness including areas such as Board paper quality, timeliness, Board meetings and engagements for the financial year. From this, a governance action plan for 2021/22 has been developed focusing on areas of continuous improvement for the Board. As part of this, the Board will have a strategy day which will focus on unregulated growth and energy transition arrangements.

Chief Executive Officer and Chief Financial Officer

Below the Board, executive responsibility rests with John Morea, Chief Executive Officer (CEO) and Mick Carmedy, Chief Financial Officer (CFO). The CEO and CFO are each employed by the Group and are not Directors of the Company although attend each Board meeting. They are supported by the Executive Committee.

Executive Committee

Day-to-day management of the Company is delegated to the Executive Committee which meets monthly and is chaired by the Chief Executive Officer and whose membership includes the Chief Financial Officer and leaders of each business unit. The Executive Committee is in turn supported by its own operational and assurance framework with defined roles and responsibilities including relevant delegated authorities.

Board and Executive Reporting

To ensure that all decision making is well-informed, transparent and balanced, careful consideration is given to information provision and flows within the governance framework. During the year the Group Company Secretary worked with Board Intelligence Limited to provide refresher training to Board and Committee paper authors on best practice paper writing to support the provision of high-quality information and effective decision making. This exercise involved reinforcing the use of best practice paper templates which seek to help focus the Board on what matters (including checks against their Section 172 duties). Refresher training on dashboard reporting (displaying key performance data and rapid insights on the overall health of the Company) was also provided to streamline reporting across the Group at a Committee level. Board information is distributed digitally, instantly and securely via the Board Intelligence platform once available.

The Group Company Secretary is responsible to the Board for the timeliness and quality of information. All Directors have access to the advice and services of the Group Company Secretary.

Conflicts of interest

With effect from 1 October 2008, the Companies Act 2006 has introduced a statutory duty on Directors to avoid conflicts of interest. During the year, the Group Company Secretary formally reviewed all the Directors' reported actual and potential conflicts of interest. The Board then considered and recorded each Director's reported actual and potential conflicts of interest.

In addition, conflicts of interest and governance are included as standing agenda items for every Board Meeting. The Group Company Secretary periodically reviews the Board protocols and governance framework to confirm that they remain fit for purpose and considers any initiatives which could strengthen the governance of the Company and decision making.

Shareholders

SGN has four supportive shareholders. They oversee the three regulated operating companies in Scotland, southern England and Northern Ireland as well as the holding company and a number of unregulated operating companies. The Board interacts with the shareholder members on a regular basis and always acts fairly with members of the Company.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Board Meetings

There were seven scheduled meetings of the Board in the year in line with the agreed plan of business for the year, and details of Director attendance can be found within their individual biographies.

In the months between full Board meetings, a Board update call provides the opportunity to discuss key business developments, and emerging issues and opportunities, with arrangements also in place should a Board decision or approval be required outside of the above times. In total there were nineteen Board meetings and calls during the year.

Scheduled meetings of the Board follow an agreed format, with agendas being developed from the Board's annual plan of business and tailored to reflect the current status of projects, strategic workstreams and the overarching operating context. Finalisation of meeting content is a collaborative process involving the Chair, Chief Executive, Chief Financial Officer and the Group Company Secretary, who ensure adequate time is allocated to support effective and constructive discussion.

Board engagement out of the Boardroom

The Board also ensures it spends time out of the Boardroom with stakeholders. During the year the Board was impacted by what physical engagement it could undertake due to social distancing but plans to resume this once social distancing permits.

Board activity

The Board splits its time between steering and supervising the organisation across strategy, performance and governance. With Board input, the Group Company Secretary has developed a focused set of priorities for the Board for the year. The aim of developing priorities is to ensure the right items come to the Board at the right frequency to help focus on the issues that matter most to the Company and ensure meeting time is used effectively. The supporting Board papers for each agenda item focus on answering the key questions on the Board's mind. In line with the Board's responsibility for the overall strategic direction of the Company, strategy related issues are discussed at every Board meeting.

During the year the Board spent a significant time considering its strategy over the next five years as part of the ongoing RIIO-GD2 and considering its response to Ofgem's draft and final determination. Throughout this process, the Board listened extensively to customers and stakeholders. We heard from over 23,000 customers and stakeholders across the Group through our comprehensive and high quality engagement programme, which included multiple face-to-face workshops, telephone interviews, meetings, surveys, webinars and quantitative research activities. In addition, our engagement via digital platforms, including our website and social media channels, reached more than one million people online.

The Business Plan is built on this feedback, which includes consideration of how a company's activities may impact both current and future stakeholders ensuring that the expectations of stakeholders in respect of SGN's economic, social and environmental impacts are integrated within, and consistent with, Strategic Pillars and matters relating to the employment, retention and development of the skilled and talented people on which the successful execution of SGN's strategy depends.

As part of this, the Board has overseen a number of other strategy-related analyses, including, but not limited to: a review of SGN's pathway to the decarbonisation of heat, covering relevant trends in policy, technology, customer and stakeholder expectations; SGN's long-term financial outlook; assessment and prioritisation of growth opportunities; and a review of SGN's key risks.

Further details of the areas which have shaped the Board agendas during 2020/21 are set out below, together with an overview of how these link to our strategic pillars (as described on page 3 of the Strategic Report).

Southern Gas Networks Plc (Registered number: 05167021)Directors' Report
for the Year Ended 31 March 2021

Board Focus Strategy	Detailed description	Link to Strategic Pillars
	Development of GD2 Business Plan and decision to appeal final determination by Ofgem - extensive review and analysis.	1,2,3
	Transformation - review of transition plans into GD2 to ensure ability to meet regulatory outputs and financial metrics	1,2,3,4,5
	Energy Futures & net-zero - Approved various energy future projects connected with the development of the Company's strategy towards the pathway to the decarbonisation of heat	1,2,3,4,5
	Environment - Approved the Environmental Action Plan and strategy	3
	Stakeholders - Review of engagement with energy policy holders on various topics including, energy transition, Covid-19 and Brexit.	1,2,3,4,5
	People and Culture - Review of Covid-19 engagement surveys to understand employee views and approval of action plans, including return to work strategies.	5
	Property - Approved development of new head office encompassing a new gas control centre.	1,2,3,4,5
	Digitalisation strategy - reviewed and approved digitalisation strategy (DS) forming part of Scotland and Southern Gas Networks plc's licence obligations.	1,2
Performance		
	Financial - review of long-term financial outlook and performance including consideration of dividend proposals, sufficient resources and approval of annual budget.	1,2,3,4,5
	Liquidity - approval of short-term liquidity measures as a result of Covid-19, including CCFF placement and deferral of dividends.	1,2,3,4,5
	Covid-19 Impact and Response Plans - extensive consideration of Covid-19 impact areas and response plans to ensure corporate objectives are met.	1,2,3,4,5
	Regulatory performance - continued Board focus and review of regulatory performance and initiatives.	1,2,3

Southern Gas Networks Plc (Registered number: 05167021)Directors' Report
for the Year Ended 31 March 2021

Board focus	Detailed description	Link to strategic pillars
	Safety performance - continued Board focus and review of safety performance and initiatives, including Board site visits.	1
	Cyber - focussed review and assurance.	1
Governance	Strategic risks - consideration of strategic risks (further details on page 5 and implementing appropriate governance, monitoring compliance and ongoing risk management.	1,2,3,4,5
	Contract strategy and approvals - various significant contracts, including strategies, considered pursuant to the Board schedule of reserved matters.	1,2,3,4,5
	Policies and certificates - approved various Company policies and compliance certificates in line with the Governance Framework, such as modern slavery.	-
	Governance - review of Board committee membership, reporting, priorities and planning and compliance with the new Corporate Governance requirements.	-
	Board effectiveness - Review of board effectiveness and action plan.	-

Key to Strategic Pillars

1. Delivering a safe and efficient service
2. Making a positive impact
3. Building a shared future
4. Creating value and growing our service
5. Focusing on talent, skills and opportunities for our people

Board Committees

In order to provide effective and focused leadership, the Board has established five standing committees with specific responsibilities. These are the Audit Committee, the Health and Safety Committee, the People and Reward Committee, the Stakeholder, Environment and Customer Committee and the Finance Committee.

Each committee's performance, constitution and terms of reference are reviewed annually to ensure they are operating effectively. The Company Secretary acts as secretary for each committee and further details are set out below.

AUDIT COMMITTEE**Membership**

The current members of the Audit Committee are Paul Jeffery (Committee Chair), Nick Salmon, Gregor Alexander, Guy Lambert, Delphine Voeltzel.

Attendees

The External Auditors are invited to attend the Audit Committee along with the Chief Financial Officer, the Head of Internal Audit & Compliance, the Group Financial Controller and the Group Accounting Manager who represent Management.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

The role of the Committee and principle responsibilities

The Audit Committee is a sub-committee of the Board. The Committee's role is to support the Board within the Governance Framework in matters relating to the integrity of Financial Reporting; relationship with the External Auditor and the effectiveness of the external audit process; effectiveness of the Internal Audit and Compliance function; and effectiveness of the System of Internal Control. The Audit Committee also reviews key regulatory filings prior to submission to Ofgem.

What the Committee has done this year

The Audit Committee held three meetings during the financial year which were scheduled in advance of Board meetings. This enabled the Chair to report on key matters discussed to the Board and, where required, recommend decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Financial reporting

- Reviewed & considered key accounting judgements, the interim and final financial results and recommended the same for approval by the Board for the annual results for the statutory and regulatory accounts.
- Reviewed and approved the goodwill impairment and carrying value judgements.

External audit

- Reviewed and considered the appointment of a new external auditor, Ernst & Young LLP.
- Monitored the independence of the external auditor.
- Reviewed the effectiveness of the external audit process and considered market trends and impacts.
- Considered the accounting, financial control and audit issues from the external auditor's report.

Internal audit

- Reviewed the outputs from the internal audit benchmarking against the Internal Auditors (IIA) Code of Practice and approved changes to the Internal Auditor Charter.
- Approved the annual audit plan and received regular updates on the delivery of the plan.

Risk management and internal controls

- Approved the annual compliance plan and received regular updates on the delivery of the plan.
- Reviewed key outcomes of all internal compliance investigations, including incidents raised via "speak up" channels to help assess risks, trends, and culture across the Company.
- Received external compliance report on compliance with standard licence condition A27 concerning business separation and approved submission to Ofgem.

Regulatory filings and governance

- Approved the debt to RAV and compliance certificates
- Monitored the level of non-audit fees and approved any new non-audit services.
- Reviewed and agreed changes to the Committee terms of reference.

Looking forward

The Committee's priorities for FY21/22 are continuing to develop and improve our internal controls and assurance processes, with input from our internal and external auditors. An external quality assessment of the Internal Audit Function is also planned for 2022.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

HEALTH AND SAFETY COMMITTEE

Membership

The current members of the Health and Safety Committee are Rob McDonald (Committee Chair), Laura Sandys Guy Lambert, Michael McNicholas and Nick Salmon.

Attendees

The Chief Executive Officer, the Network & Safety Director, the Group Head of Safety & Environment and the Group Accounting Manager also attend the Health and Safety Committee meetings to represent Management.

The role of the Committee and principle responsibilities

The Health and Safety Committee is a sub-committee of the Board. The Health and Safety Committees role is to support the Board by fulfilling its health and safety responsibility to employees and members of the public.

The Health and Safety Committee is responsible for:

- ensuring that the Company's health and safety policy statement remain fit for purpose and monitoring the execution of those policy statements by the Company;
- approving and monitoring the Company's Safety and Health Assurance Plan;
- setting engineering process safety, occupational health and safety targets to improve company performance;
- monitoring health and safety performance against targets and key improvement areas by means of suitable and sufficient leading and lagging key performance indicators; and
- providing Board leadership to the Company's Executive Committee to drive continuous and sustained improvement in all aspects of safety and health performance.

What the Committee has done this year

The Health and Safety Committee held six meetings during the financial year, which were scheduled in advance of Board meetings. This enabled the Chair to report on key matters discussed to the Board and, where required, recommend decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Performance

- Reviewed and approved the process safety and occupational health and safety targets for the financial year and monitored performance against these.
- Reviewed and approved the safety compliance and assurance plans, including external assurance activity.
- Reviewed the impact of Covid-19 on safety performance and agreed revised targets in light of circumstances.
- Reviewed the Company's winter readiness and road traffic improvement plan.
- Reviewed progress against the safety culture and mental health programme.

Governance

- Reviewed and approved the Safety, Health and Environment Policy statement for FY20/21.
- Reviewed and agreed changes to the Committee terms of reference.

Strategy

- Reviewed the Company's approach to Covid-19 health and safety matters.
- Reviewed the adoption of technology to help monitor health and safety across the Company.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Looking forward

The Committee's priorities for FY21/22 are continuing to drive health and safety improvements ensuring that the Company achieves its commitment to getting everyone home safe and well. FY21/22 will see increasing focus on safe day performance which will now be monitored, and performance assessed, against 7 days (previously 5 days). There is also planned a further drive in reporting and performance improvements for mental health and wellbeing.

PEOPLE AND REWARD COMMITTEE

Membership

The current members of the People and Reward Committee are Michael McNicholas (Committee Chair), Nick Salmon, Gregor Alexander, Charlotte Brunning, Guy Lambert.

Attendees

The Chief Executive Officer, the HR & Services Director and the Head of Employee Relations, Policy & Rewards also attend the People and Reward Committee meetings to represent Management.

The role of the Committee and principle responsibilities

The People and Reward Committee is a sub-committee of the Board. The People and Reward Committee's role is to support the Board by ensuring:

- remuneration policy and practices of the Company reward fairly and responsibly, with a clear link to corporate and individual performance, having regard to statutory and regulatory requirements;
- talent and succession strategy for the Company's Executive is suitable for the Company's long-term success;
- diversity and inclusion plays a key role across the Company; and
- employee feedback is listened to and acted on.

What the Committee has done this year

The People and Reward Committee held four meetings during the financial year, which were scheduled in advance of Board meetings. This enabled the Chair to report on key matters discussed to the Board and, where required, recommend decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Strategy

- Approved the annual salary review of all employees for cost of living increases
- Reviewed and approved changes to the executive remuneration policy framework.
- Reviewed the short-term incentive plan (STIP) and long-term incentive plan (LTIP) framework for the Financial Year ensuring these measured both financial and non-financial performance.

Performance

- Approved the performance assessments for STIP and LTIP for the prior Financial Year.
- Considered impacts and adjustments to the STIP for the year due to Covid-19.
- Reviewed and approved personal objectives for the Chief Executive Officer and Chief Financial Officer and assessed prior year performance.

Governance

- Approved a thank you payment to all employees (excluding the Executive) for their commitment and hard work during Covid-19.
- Reviewed the Gender Pay Gap Report.
- Approved becoming a Living Wage employer.
- Reviewed and agreed changes to the Committee terms of reference.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Looking forward

The Committee's priorities for FY21/22 are to ensure the talent and succession strategy for the Company's Executive is suitable for the Company's long-term success and diversity and inclusion plays a key role across the group. The committee will also review feedback from employees taking part in the Company's bi-annual employee engagement survey and monitor performance against an approved action plan.

FINANCE COMMITTEE

Membership

The current members of the Finance Committee are Charlotte Brunning (Committee Chair), Paul Jeffery, Gregor Alexander, Guy Lambert, Delphine Voeltzel.

Attendees

The Chief Financial Officer and Group Treasurer also attend the Finance Committee meetings to represent Management.

The role of the Committee and principle responsibilities

The Finance Committee is a sub-committee of the Board.

The Finance Committee's role is to support the Board by determining:

- distribution proposals and strategy including forecast distributions;
 - financing and refinancing strategy and proposed debt issuance;
 - financial risk management strategy;
 - credit rating strategy;
 - a policy concerning the operation of bank accounts and facilities, including appointment of authorised personnel to those accounts and facilities; and
 - a policy of granting guarantees, indemnities, any type of parent-company support or security interest.
- In addition, the Finance Committee will review and approve investments or transactions where the Committee has been delegated authority by the Board to do so.

What the Committee has done this year

The Finance Committee held ten meetings during the financial year of which six were additional, planned to consider Covid-19 impacts and Ofgem's draft and final determination of RIIO-GD2. The Chair reports on key matters discussed to the Board and, where required, recommend decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Strategy

- Reviewed and approved the EMTN update and Bond Issuance.
- Reviewed and approved a counterparty liability strategy.
- Received regular updates from the GD2 Management team on finance-ability, together with rating agency outlooks.
- Considered and approved a financing and inflation strategy to support RIIO-GD2 delivery.
- Reviewed and approved changes to the Company's defined benefit pension scheme together with an engagement strategy.

Governance

- Reviewed and approved a commercial bid for a biomethane opportunity with Thames Water
- Discussed the LIBOR reform.
- Reviewed and approved the Company's bank and treasury mandates.
- Reviewed and agreed changes to the Committee terms of reference.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report for the Year Ended 31 March 2021

Performance

- Reviewed the liquidity of the Company and Covid-19 relief measures.
- Considered distribution proposals before making recommendations to the Board.

Looking forward

The Committee's priorities for FY21/22 are to monitor the implementation of financial and risk management strategies approved in FY20/21 to ensure credit ratings are maintained within target rating levels.

STAKEHOLDER, ENVIRONMENT AND CUSTOMER COMMITTEE

Membership

The current members of the Stakeholder, Environment and Customer Committee are Laura Sandys (Committee Chair), Charlotte Brunning, Guy Lambert, Rob McDonald, Michael McNicholas

Attendees

The Chief Executive Officer and the Director of Stakeholder and Communications also attend the Stakeholder, Environment & Customer Committee meetings to represent Management.

The role of the Committee and principle responsibilities

The Stakeholder, Environment and Customer Committee is a sub-committee of the Board. The Stakeholder, Environment and Customer Committee's principle role is to ensure the Company has due regard to:

- stakeholder, environmental and customer (SEC) interests;
- the need to foster relationships with suppliers, customers and others; and
- the Company's impact (including the impact of any principal decisions taken by the Group) on the broader community and environment.

The Committee also supports with Board oversight for the identification of stakeholder, environmental and customer opportunities and risks and emerging Environmental, Social and Governance issues.

What the Committee has done this year

The Stakeholder, Environment and Customer Committee held three meetings during the financial year, which were scheduled in advance of Board meetings. This enabled the Chair to report on key matters discussed to the Board and, where required, recommend decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Strategy

- Reviewed the remit and principle duties and future ambition of Stakeholder, Environment & Customer Committee.
- Considered ESG reporting and framework options.
- Reviewed and provided feedback on the customer strategy for RIIO-GD2.
- Reviewed and approved the Environment Strategy.
- Reviewed performance against GD1 and GD2 Ofgem reporting requirements.
- Review and approved the Environmental policy and targets for FY21.
- Reviewed the Company's approach to S172 of the Companies Act 2006 in its annual report.
- Reviewed and agreed changes to the Committee terms of reference.

Southern Gas Networks Plc (Registered number: 05167021)Directors' Report
for the Year Ended 31 March 2021**Looking forward**

The Committee priority for FY21/22 is to select and recommend to the Board the right ESG strategy and reporting framework which underpins the long-term success of the Company, whilst continuing to ensure stakeholder interests are listened to and acted.

Attendance at Board and Board Committee meetings

The attendance of the Board of Directors and the Board Committees during the year is as set out below.

	Board meetings		Audit Committee meetings		People and Reward Committee meetings	
	Attended	Possible	Attended	Possible	Attended	Possible
Gregor Alexander	19	19	3	3	4	4
Robert McDonald	19	19	3	3	-	-
Charlotte Brunning	19	19	-	-	4	4
Michael McNicholas	19	19	-	-	4	4
Delphine Voeltzel*	14	14	2	2	-	-
Guy Lambert	15	19	3	3	2	4
Paul Jeffery	19	19	3	3	-	-
Nicholas Salmon	19	19	3	3	-	-
Laura Sandys	19	19	-	-	-	-

	Health and Safety Committee meetings		Finance Committee meetings		Stakeholder, Environment and Customer Committee meetings	
	Attended	Possible	Attended	Possible	Attended	Possible
Gregor Alexander	-	-	9	9	-	-
Robert McDonald	-	-	-	-	3	3
Charlotte Brunning	-	-	9	9	3	3
Michael McNicholas	-	-	-	-	3	3
Delphine Voeltzel*	-	-	6	6	-	-
Guy Lambert	3	6	6	9	1	3
Paul Jeffery	-	-	9	9	-	-
Nicholas Salmon	6	6	-	-	-	-
Laura Sandys	6	6	-	-	3	3

* Delphine Voeltzel joined the Board in July 2020.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

Directors' and Senior Executives' Biographies and Responsibilities as at 31 March 2021

Nick Salmon, Chair, Non-executive Director

Nick joined the Board in March 2019 as a Teachers' nominee and was appointed the Chair of SGN in March 2021. He is also currently Chair of South East Water Ltd. Previously he was the Senior Independent Director at both United Utilities plc and Elementis plc, a Non-executive Director at Interserve plc and CEO of Cookson Group plc and Babcock International Group plc. Nick is member of the Audit Committee, the People and Reward Committee and the Health and Safety Committee.

Gregor Alexander, Non-executive Director

Gregor joined the Board at its inception in August 2004. He is Finance Director of SSE plc and previously worked with the accountancy firm Arthur Andersen. He is also Non-Executive Director of Stagecoach Group plc and Director of Scottish and Southern Energy Power Distribution Limited and related entities. He is member of the Audit Committee, the Finance Committee and the People and Reward Committee.

Robert McDonald, Non-executive Director

Robert joined the Board in July 2006. He is Managing Director of SSEN Transmission and has previously worked with the industry's regulatory body. He is Director of Scottish and Southern Energy Power Distribution Limited and related entities and Director of Energy Networks Association Limited. Robert serves as the Chair of the Health and Safety Committee. He is also member of the Stakeholder, Environment and Customer Committee.

Charlotte Brunning, Non-executive Director

Charlotte joined the Board in May 2018. She is a member of the EMEA Infrastructure and Natural Resources team and had been with Ontario Teachers' since 2015. She has been involved in a number of direct investments, including London City Airport and SGN Smart. Charlotte holds a B.Sc. from the London School of Economics and an MBA from the London Business School. She is Director of Galaxy Pipeline Assets Topco Limited, Apple Newco Limited, Western Topco Limited and Rubicon Topco Limited. Charlotte serves as the Chair of the Finance Committee. She is also member of the People and Reward Committee and the Stakeholder, Environment and Customer Committee.

Delphine Voeltzel, Non-executive Director

Delphine joined the Board in July 2020. A Director at OMERS Infrastructure, she is responsible for the origination, execution and management of investments in the utilities and renewables sectors across Europe. She previously worked with the investment bank Rothschild. Delphine is also Non-Executive Director of NET4GAS. She is member of the Audit Committee and the Finance Committee.

Guy Lambert, Non-executive Director

Guy joined the Board in October 2016. He joined the Abu Dhabi Investment Authority (ADIA) in 2008 and currently serves as the Head of Utilities. He is responsible for sourcing and executing new investments in the utilities sector and overseeing the existing utilities portfolio. Guy is a member of the Audit Committee, the Finance Committee, the People and Reward Committee, the Stakeholder, Environment and Customer Committee and the Health and Safety Committee.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

Michael McNicholas, Non-executive Director

Michael joined the Board in June 2019. He is Managing Director, Asset Management in OMERS Infrastructure and responsible for the active management of investments, with a focus on Europe. Prior to joining OMERS, Michael was CEO of Ervia Group with responsibility for Ireland's Gas Networks and the national Water Utility. Michael also served as Group CEO of NTR, a sustainable infrastructure company investing in renewables, and recycling in Europe and the USA. He is Director of Thames Water Limited and related entities, Kemble Water Holdings Ltd and related companies, Ellevio AB and related entities and Caruna OY and related entities. Michael serves as the Chair of the People and Reward Committee. He is also member of the Stakeholder, Environment and Customer Committee and the Health and Safety Committee.

Peter McCosker, Alternate Director

Peter joined the SGN Board in 2019. Peter is a Portfolio Manager in the Infrastructure Division of the Abu Dhabi Investment Authority which he joined in 2014. In this role, Peter is responsible for portfolio company asset management and transaction execution. He has significant utilities experience in the United Kingdom, Australia and the United States. Peter is Director of Oasis Infrastructure Investments Ltd, Alternate Director of Tawreed Investments Limited and Blue Globe A 2013 Limited, Director and Vice President of Black Buffalo B 2014 Inc.

Charles Thomazi, Alternate Director

Charles joined the board in October 2017 and leads the EMEA Infrastructure team in Teachers' Infrastructure Group. He attends board meetings as a substitute to Charlotte Brunning. Charles is Director of Ontario Teachers' Pension Plan (OTPP), Galaxy Pipelines Asset TopCo Limited, Apple NewCo Limited, Sauna HoldCo Limited and related entities and Western TopCo Limited.

Paul Jeffery, Statutory Independent Non-executive Director

Paul joined the Board in January 2014. Previously he ran the European Power, Utility and Infrastructure Investment Banking Sector team for Barclays. Non-Executive Director of London Power Networks Ltd, South-Eastern Power Networks Ltd, Eastern Power Networks Ltd and UK Power Networks (IDNO) Ltd all forming part of the UK Power Networks group. Paul is also a director and shareholder of P&G Property Limited. Paul is the Chair of the Audit Committee and a member of the Finance Committee.

Laura Sandys, Statutory Independent Non-executive Director

Laura joined the board in October 2018. She was a member of the Energy and Climate Change Select Committee and co-founder of POWERful Women which promotes women's role in the energy sector. She has been appointed a member of the Government's CCUS Council and is a Member of Imperial College's Centre for Carbon Capture and Storage Advisory Group. Laura is Co-ordinator for the Reshaping Regulation Programme with Imperial College and Energy Systems Catapult, Non-Executive Director of Energy System Catapult Limited, Chair for the Energy Digitalisation Taskforce, Non-Executive Director for Antika PLC and Chair for the Food Foundation CIC. Laura serves as the Chair of the Stakeholder, Environment and Customer Committee and she's also member of the Health and Safety Committee.

John Morea, Chief Executive Officer

John joined the Company in May 2005 from SSE plc. He has over 30 years' experience in the energy industry. John is a companion of the Institute of Gas Engineers and Managers, a member of the Institute of Engineering and Technology and holds an MBA. John is also a Director of Thames Water Utilities Limited and Energy Networks Association Limited.

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Report
for the Year Ended 31 March 2021

Mick Carmedy, Chief Financial Officer

Mick joined the Company in January 2018. Mick was CFO of Southern Water, the regulated water business, for five years prior to joining. Mick has also worked at United Utilities and Thames Water in a wide variety of roles. Mick is also Director of Murphy Asset Services Limited.

Nicola Shand, Director of Legal Services, Company Secretary

Nicola joined the Board as Company Secretary in July 2011. Nicola is Director of Legal Services and is responsible to the Board for compliance with Board procedures and for advising and keeping the Board up to date on all corporate governance developments. Nicola is also Non-Executive Director of FYLD Limited.

DISCLOSURE IN THE STRATEGIC REPORT

Details on how the directors have had regard to the need to foster the Company's business relationships with suppliers, customers and others, and the effect of that regard on the principal decisions taken by the Company during the financial year can be found in the strategic report.

AUDITOR

Each of the Directors at the date of this report confirms that:

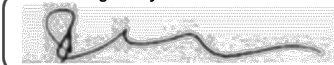
1) So far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and

2) The Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

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

The auditor, Ernst & Young LLP, will be proposed for re-appointment at the forthcoming Annual General Meeting.

BY ORDER OF THE BOARD:

DocuSigned by:

.....906CP4A85DC24B1:.....
Nicola Shand - Secretary

Date: 20 July 2021
.....

Southern Gas Networks Plc (Registered number: 05167021)

Directors' Responsibilities Statement
for the Year Ended 31 March 2021

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

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

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

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

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

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

We confirm that to the best of our knowledge:

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

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.

Report of the Independent Auditor to the Members of Southern Gas Networks Plc

Opinion

We have audited the financial statements of Southern Gas Networks Plc for the year ended 31 March 2021 which comprise the Profit and Loss Account, the Statement of Comprehensive Income, the Statement of Changes in Equity, the Balance Sheet, Statement of Cash Flows, and the related notes 1 to 26 including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

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

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

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

- Due to groups cash pooling arrangements the company is dependent on a letter of support provided by its ultimate parent company, Scotia Gas Networks Limited. In assessing the company's ability to continue as a going concern we therefore obtained a copy of the letter of support and considered the group's going concern assessment and its ability to provide that support.
- The following are the procedures we performed over that group assessment which supports the company assessment to the extent necessary to conclude on the company's ability to continue as a going concern:
 - Understanding and walking through management's process for and controls related to assessing going concern including discussion with management to ensure all key factors were taken into account;
 - Obtaining and performing mechanical integrity testing on management's going concern model, which is for the period to 31 July 2022, and which includes details of facilities available, covenant calculations, and the results of management's scenario planning;
 - Comparing to the debt agreements both the maturity profile of the debt and the covenants that are required to be met within the going concern period;
 - Agreeing the forecasts underpinning the going concern model to the Board-approved budget for FY 2022 and the Board-approved strategic plan;

Report of the Independent Auditor to the Members of Southern Gas Networks Plc

- Challenging how these forecasts have been revised to reflect any impact of COVID-19; challenging key assumptions within the forecasts with the assistance of our regulatory specialist team and with reference to the GD2 regulatory regime;
 - Evaluating management's historical forecasting accuracy by comparing budgets to actual results; Assessing the consistency of the going concern assessment with information obtained from other areas of the audit, such as the goodwill impairment testing;
 - Performing reverse stress testing on the going concern model by understanding what reduction in EBITDA would be required before liquidity is exhausted and considering the likelihood of the events required to breach the covenants;
 - Evaluating the Group's ability to undertake mitigating actions and considering whether those actions are within the Group's control and the timing of when they could be implemented; and
- Reviewing the going concern disclosures in the annual report to ensure that they are in accordance with the reporting standards.

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

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

Overview of our audit approach

Key audit matters

- Valuation of goodwill
- Valuation of the defined benefit obligation

Materiality

Overall materiality of £9.7m which represents 4% of the Company's profit before tax.

Tailoring the scope

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

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Report of the Independent Auditor to the Members of
Southern Gas Networks Plc

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Valuation of goodwill (£197m, PY comparative £203m)</p> <p>Refer to the Audit Committee Report (page 10); Accounting policies (page 60); and Note 10 of the Financial Statements (page 75).</p> <p>There is a risk that the Southern Gas Networks plc Cash Generating Unit ("CGU") may not achieve the anticipated business performance to support the carrying value of the underlying assets, leading to an impairment charge that has not been recognised by management.</p> <p>Significant judgement is required in determining the future cash flows and therefore the recoverable amounts of the CGU.</p> <p>If these judgements are not appropriate, then this increases the risk that goodwill could be incorrectly valued.</p>	<p>We performed the following audit procedures:</p> <ul style="list-style-type: none"> - Performed walkthrough procedures to verify our understanding of the process, identifying key controls; - Understood how management assessed the recoverable amount and compared this approach to what we would expect for an industry participant; - Checked management's CGU carrying value composition for consistency with the recoverable amount methodology; - Engaged our modelling experts to test the integrity of the Board approved Strategic Model which underpins the impairment model and identify the key assumptions; - Tested the discounted cashflow ("DCF") in the impairment model for clerical accuracy; - Utilised EY valuation and regulatory specialists to audit the key assumptions and inputs to the impairment model. This included comparing the discount rate and terminal value to our independent range, as well as agreeing GD2 inputs to the Ofgem approved model. It also included assessing the reasonableness of assumptions in respect of outperformance in GD2 and future regulatory periods, and how climate and sustainability trends could impact the business in the future; - Compared forecasts and assumptions used in the prior year analysis (where applicable) to the actual performance to assess management's forecasting accuracy; - Considered if any contradictory evidence existed, including comparing the implied RAV multiple to recent regulatory transactions; - Performed sensitivity analysis on certain key assumptions in the model including the discount rate; and - Considered compliance of the related goodwill disclosures under FRS 102. 	<p>Following our audit challenge, management made changes to the impairment model. However, these changes did not impact the overall impairment assessment.</p> <p>All assumptions used in valuing the goodwill were within an acceptable range.</p> <p>Our year end audit procedures did not identify evidence of material misstatement regarding the carrying value of goodwill.</p> <p>We consider the disclosures to be appropriate and in accordance with FRS 102.</p>

Report of the Independent Auditor to the Members of
Southern Gas Networks Plc

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Valuation of the defined benefit obligation (£562m, PY comparative £470m)</p> <p>Refer to the Audit Committee Report (page 11); Accounting policies (page 66); and Note 23 of the Financial Statements (page 84)</p> <p>The Company operates a defined benefit pension scheme. Significant estimates and judgements are made in valuing the Company's pension obligation.</p> <p>Due to the quantum of the underlying balance, relatively small changes in key assumptions could have a significant effect on the calculation of the carrying value of the Company's pension obligation. Key assumptions include salary increases, the mortality rate, the discount rate and the RPI and CPI inflation rates.</p> <p>There is a risk that if one (or several assumptions in aggregate) are outside of an acceptable range, the defined benefit obligation would be incorrectly valued which would have a significant impact on the Company's financial position.</p>	<p>We performed the following audit procedures:</p> <ul style="list-style-type: none"> - Performed walkthroughs of the pension process to verify our understanding and identify the key controls in place around the valuation assumptions; - Assessed the independence, objectivity and competence of the external actuarial specialist; - With support from our pension actuarial specialists, we independently benchmarked the key assumptions used in valuing the defined benefit obligation against an EY range derived from market data. This included salary increases, mortality rate, the discount rate, and RPI and CPI inflation rates; - Performed tests of detail for a sample of the participant data used by the external actuaries to confirm the completeness and accuracy of this data; and <p>Considered compliance of the related disclosures under FRS 102.</p>	<p>Based on the audit procedures performed, we consider the valuation of the Company's defined benefit obligation for the year ended 31 March 2021 to be appropriate.</p> <p>All assumptions used in valuing the obligation within an acceptable EY range.</p> <p>We consider the disclosures to be appropriate and in accordance with FRS 102.</p>

Our application of materiality

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

Materiality

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

Report of the Independent Auditor to the Members of Southern Gas Networks Plc

We determined materiality for the Company to be £9.7m which represents 4% of Company's profit before tax. We believe that profit before tax provides us with the most relevant performance measure to the stakeholders of the entity and therefore have used this as the basis for determining materiality.

Performance materiality

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

On the basis of our risk assessments, together with our assessment of the Company's overall control environment, our judgement was that performance materiality was 50% of our planning materiality, namely £4.9m. We have set performance materiality at this percentage due to the additional complexities associated with a first-year audit for EY and the number and size of the misstatements identified by the predecessor auditor in the prior year.

Reporting threshold

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

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.5m, which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

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

Other information

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

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

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

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

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

Report of the Independent Auditor to the Members of Southern Gas Networks Plc

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

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

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

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 43, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

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

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

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Company and determined that the most significant are those that relate to the reporting framework (FRS 102 and the Companies Act 2006) and the local tax legislation. In addition, we concluded that there are certain significant laws and regulations which may have an effect on the determination of the amounts and disclosures in the financial statements being laws and regulations relating to health and safety, environmental protection and employee matters, notably pensions. In addition, the Company operates in a regulated market; it is subject to regulations from the national regulatory authorities in Great Britain.

Report of the Independent Auditor to the Members of
Southern Gas Networks Plc

- We understood how the Company is complying with those frameworks by making enquiries of management, internal audit and those responsible for legal and compliance procedures and the Company secretary. We corroborated our enquiries through our review of Board minutes, papers provided to the Audit Committee and correspondence received from regulatory bodies and noted that there was no contradictory evidence.
- We assessed the susceptibility of the Company's financial statements to material misstatement, including how fraud might occur by meeting with management from various parts of the business to understand where it considered there was susceptibility to fraud. We considered the programmes and controls that the Company has established to address risks identified, or that otherwise prevent, deter and detect fraud; and how senior management monitors those programmes and controls. Where the risk was considered to be higher, we performed audit procedures to address each identified fraud risk. These procedures included using data analysis for testing journal entries that met our defined risk criteria based on our understanding of the business and challenging the assumptions and judgements made by management in areas where judgement is required including those referred to in the key audit matters section above.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved understanding management's internal controls over compliance with laws and regulations; enquiry of legal counsel, management and internal audit; and reviewing internal audit reports and whistleblowing logs.

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

Other matters we are required to address

- Following the recommendation from the audit committee we were appointed by the Company on 30 June 2020 to audit the financial statements for the year ending 31 March 2021 and subsequent financial periods.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Company and we remain independent of the Company in conducting the audit.
- The audit opinion is consistent with the additional report to the audit committee.

Use of our report

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

Ernst & Young LLP

Andy Williams (Senior Statutory Auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

Date: 20 July 2021

Southern Gas Networks Plc (Registered number: 05167021)Profit and Loss Account
for the Year Ended 31 March 2021

		2021	2020
	Notes	£m	as restated £m
TURNOVER		806	818
Operating costs		<u>(461)</u>	<u>(445)</u>
OPERATING PROFIT		345	373
Interest receivable and similar income	4	5	3
Interest payable and similar expenses	5	<u>(107)</u>	<u>(117)</u>
PROFIT BEFORE TAXATION	6	243	259
Tax on profit	7	<u>(47)</u>	<u>(111)</u>
PROFIT FOR THE FINANCIAL YEAR		<u>196</u>	<u>148</u>

The above results relate to continuing operations in both the current year and previous year.

Southern Gas Networks Plc (Registered number: 05167021)Statement of Comprehensive Income
for the Year Ended 31 March 2021

	2021	2020
		as restated
Notes	£m	£m
PROFIT FOR THE YEAR	196	148
OTHER COMPREHENSIVE (LOSS)/INCOME		
(Loss)/Gain arising on cash flow hedges	(1)	1
Remeasurement on net pension asset	(41)	82
Income tax relating to components of other comprehensive (loss)/income	<u>8</u>	<u>(16)</u>
OTHER COMPREHENSIVE (LOSS)/INCOME FOR THE YEAR, NET OF INCOME TAX	<u>(34)</u>	<u>67</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	<u><u>162</u></u>	<u><u>215</u></u>

Southern Gas Networks Plc (Registered number: 05167021)Balance Sheet
31 March 2021

		2021	2020
	Notes	£m	as restated £m
FIXED ASSETS			
Intangible assets	10	220	230
Tangible assets	11	<u>4,743</u>	<u>4,602</u>
		<u>4,963</u>	<u>4,832</u>
CURRENT ASSETS			
Debtors	12	74	76
Short term deposits	13	97	82
Cash at bank	14	<u>2</u>	<u>3</u>
		173	161
CREDITORS			
Amounts falling due within one year	15	<u>(229)</u>	<u>(453)</u>
NET CURRENT LIABILITIES		<u>(56)</u>	<u>(292)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		4,907	4,540
CREDITORS			
Amounts falling due after more than one year	16	(2,972)	(2,724)
PROVISIONS FOR LIABILITIES	19	(592)	(607)
DEFERRED INCOME	20	(263)	(244)
PENSION ASSET	23	<u>179</u>	<u>213</u>
NET ASSETS		<u>1,259</u>	<u>1,178</u>

Southern Gas Networks Plc (Registered number: 05167021)Balance Sheet - continued31 March 2021

		2021	2020
	Notes	£m	as restated £m
CAPITAL AND RESERVES			
Called up share capital	21	160	160
Hedging reserves	22	-	1
Profit and loss account	22	<u>1,099</u>	<u>1,017</u>
SHAREHOLDERS' FUNDS		<u>1,259</u>	<u>1,178</u>

The financial statements were approved by the Board of Directors and authorised for issue on 20 July 2021 and were signed on its behalf by:

DocuSigned by:

Nick Salmon

.....B044C85BC5E1463.....

Nicholas Robin Salmon (Chair) - Director

Southern Gas Networks Plc (Registered number: 05167021)Statement of Changes in Equity
for the Year Ended 31 March 2021

	Called up share capital £m	Profit and loss account £m	Hedging reserves £m	Total equity £m
Balance at 1 April 2019	160	860	-	1,020
Prior year adjustment	-	(4)	-	(4)
As restated	160	856	-	1,016
Profit for the year	-	148	-	148
Other comprehensive income	-	66	1	67
Total comprehensive income	-	214	1	215
Dividends	-	(53)	-	(53)
Balance at 31 March 2020	160	1,017	1	1,178
Profit for the year	-	196	-	196
Other comprehensive income	-	(33)	(1)	(34)
Total comprehensive income	-	163	(1)	162
Dividends	-	(81)	-	(81)
Balance at 31 March 2021	160	1,099	-	1,259

Southern Gas Networks Plc (Registered number: 05167021)Cash Flow Statement
for the Year Ended 31 March 2021

	Notes	2021 £m	2020 as restated £m
Cash flows from operating activities			
Cash generated from operations	1	456	525
Interest paid		(104)	(102)
Tax paid		<u>(45)</u>	<u>(81)</u>
Net cash from operating activities		<u>307</u>	<u>342</u>
Cash flows from investing activities			
Purchase of intangible fixed assets		(3)	(3)
Purchase of tangible fixed assets		(262)	(312)
Customer contributions received		25	21
Interest received		<u>-</u>	<u>(1)</u>
Net cash used in investing activities		<u>(240)</u>	<u>(295)</u>
Cash flows from financing activities			
Issue of debt		250	100
Repayment of debt		(215)	(10)
Payments of financial instruments		(7)	(9)
Dividends paid		<u>(81)</u>	<u>(53)</u>
Net cash (used in)/ from financing activities		<u>(53)</u>	<u>28</u>
		<u> </u>	<u> </u>
Increase in cash and cash equivalents		14	75
Cash and cash equivalents at beginning of year	2	85	10
		<u> </u>	<u> </u>
Cash and cash equivalents at end of year	2	<u>99</u>	<u>85</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Cash Flow Statement
for the Year Ended 31 March 2021**1. RECONCILIATION OF PROFIT BEFORE TAXATION TO CASH GENERATED FROM OPERATIONS**

	2021	2020 as restated
	£m	£m
Profit before taxation	243	259
Depreciation charges	116	113
Loss on disposal of fixed assets	5	5
Amortisation of deferred income	(6)	(6)
Amortisation charges	13	14
Increase/(decrease) in provisions	1	-
Finance costs	107	117
Finance income	(5)	(3)
	474	499
Decrease in trade and other debtors	4	4
(Decrease)/increase in trade and other creditors	(22)	22
Cash generated from operations	456	525

2. CASH AND CASH EQUIVALENTS

The amounts disclosed on the Cash Flow Statement in respect of cash and cash equivalents are in respect of these Balance Sheet amounts:

Year ended 31 March 2021

	31.3.21	1.4.20
	£m	£m
Cash and cash equivalents	2	3
Short term deposits	97	82
	99	85

Year ended 31 March 2020

	31.3.20	1.4.19
	£m	£m
Cash and cash equivalents	3	10
Short term deposits	82	-
	85	10

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Cash Flow Statement
for the Year Ended 31 March 2021**3. ANALYSIS OF CHANGES IN NET DEBT**

	At 1.4.20 £m	Cash flow £m	At 31.3.21 £m
Net cash and cash equivalents			
Cash at bank	3	(1)	2
Short term deposits	<u>82</u>	<u>15</u>	<u>97</u>
	<u>85</u>	<u>14</u>	<u>99</u>
 Debt			
Debts falling due within 1 year	(215)	215	-
Debts falling due after 1 year	<u>(2,698)</u>	<u>(253)</u>	<u>(2,951)</u>
	<u>(2,913)</u>	<u>(38)</u>	<u>(2,951)</u>
 Total	<u><u>(2,828)</u></u>	<u><u>(24)</u></u>	<u><u>(2,852)</u></u>

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES

General information and basis of preparation

Southern Gas Networks Plc is a private company limited by shares and is incorporated in England and Wales under the Companies Act 2006. The address of the registered office is St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ, United Kingdom. The Company's principal activity is the development, administration, maintenance and operation of the South and South East of England gas distribution system and the supply of gas transportation services. The nature of the Company's operations is set out in the Strategic Report.

The financial statements have been prepared under the historical cost convention, modified to include certain items at fair value, and in accordance with Financial Reporting Standard 102 - 'The Financial Reporting Standard applicable in the United Kingdom and Republic of Ireland' (FRS 102) issued by the Financial Reporting Council. There were no material departures from that standard.

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise judgement in applying the accounting policies.

The functional currency of Southern Gas Networks Plc is considered to be pound sterling because that is the currency of the primary economic environment in which the Company operates. Amounts are expressed in millions of pounds except where noted otherwise.

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks Limited and the financial statements of the Company are included in the consolidated financial statements of Scotia Gas Networks Limited which can be obtained from St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ, United Kingdom.

The group has taken advantage of the exemption afforded by FRS 102.33.1A not to disclose transactions between wholly owned members of the group.

The company is a qualifying entity as defined by FRS 102 and has taken advantage of the following exemptions available to qualifying entities which are relevant to its financial statements:

- the requirement to disclose information about key management personnel compensation;
- the disclosure requirements of Section 11 paragraphs 11.42, 11.44, 11.45, 11.47, 11.48(a)(iii), 11.48(a)(iv), 11.48(b) and 11.48(c) in respect of financial instruments of the parent (as equivalent disclosures are included in respect of the consolidated financial statements).

The following principal accounting policies have been applied:

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES - continued

Going concern

The Company's accounts have been prepared on a going concern basis.

The directors have forecast cash flows of the company for the next twelve months (the going concern period) and have obtained a support letter from Scotia Gas Networks Limited confirming that it can and will support the Company in meeting its liabilities throughout the going concern period.

In assessing the ability of the company to rely on this support the directors have considered the impact of COVID-19 on the Group and the going concern assessment undertaken at the Scotia Gas Networks Limited group level, the conclusion of which is that even under severe but plausible downside scenarios there is headroom in relation to both liquidity and covenants.

Consequently, the directors believe that the Company will be able to meet its liabilities as they fall due and will have adequate resources to continue in operational existence for 12 months from the date of approval of this report. Accordingly, the directors continue to adopt the going concern basis in preparing the financial statements.

Turnover

Turnover is stated net of value added tax and is attributable to the continuing activity of transportation of natural gas and the provision of related services. Turnover is recognised to the extent that there is a right to consideration and is recorded at the value of the consideration due.

Intangible assets - goodwill

Goodwill arising on the acquisition of businesses, representing any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight line basis over its useful economic life, which is estimated to be 50 years. Provision is made for any impairment, and it is tested on an annual basis at each balance sheet date.

Intangible assets - software

Software assets are included at cost, net of amortisation and any provision for impairment. Amortisation is provided on a straight-line basis over their estimated useful economic life of 3 to 10 years. The Company's intangible assets have a remaining useful economic life ranging between 1 - 7 years.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**1. ACCOUNTING POLICIES - continued****Tangible fixed assets**

Tangible fixed assets are stated at cost, net of depreciation and any provision for impairment. The cost is the purchase cost of the asset, together with any directly attributable costs incurred in bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. In accordance with Ofgem guidance for gas transportation licensees and as allowable under FRS 102, costs include an element of capitalised overheads which are, as far as reasonably practicable, allocated in accordance with the activities which lead to the generation of the assets. These costs are directly attributable to the associated assets.

Depreciation is recognised on all tangible fixed assets, other than freehold land, at rates calculated to depreciate the cost or valuation, less estimated residual value, of each asset on a straight-line basis over its expected useful life, as follows:

Freehold buildings:	Up to 50 years
Leasehold land and buildings:	Over the shorter of lease term and 50 years
Plant and machinery:	
-Mains and services:	55 to 65 years
-Regulating equipment:	30 to 50 years
-Gas storage:	40 years
-Motor vehicles and office equipment:	3 to 10 years
Site remediation costs are depreciated over the life of the asset.	

Replacement expenditure is capitalised within mains and services and depreciated accordingly above.

Residual value represents the estimated amount which would currently be obtained from disposal of an asset, after deducting estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

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

Fixed Asset Investments

Fixed asset investments are stated at cost less a provision for any impairment in value. Costs of the investments include all costs directly related to the acquisition of the investments.

Investments are reviewed for impairment if events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairments are calculated such that the carrying value of the fixed asset investment is the lower of its cost or recoverable amount. Recoverable amount is the higher of its net realisable value and its value in use.

Customer contributions

Customer contributions for connections to the network and for replacement expenditure diversions are treated as capital grants. They are accounted for as deferred income and released to depreciation on a straight line basis over the estimated life of the related asset.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**1. ACCOUNTING POLICIES - continued****Financial instruments**

FRS 102 sections 11 and 12 give an accounting policy choice for financial instruments. The Company has chosen to apply the recognition and measurement provisions of IAS 39 (as adopted for use in the EU) and the disclosure requirements of FRS 102 in respect of financial instruments.

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument.

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

The Company's funding, liquidity and exposure to interest rate risks are managed within a framework of policies and guidelines authorised by the Board of Directors. In accordance with these policies financial derivative instruments are used to manage interest rate and currency exposure.

Where appropriate these instruments are recorded at fair value and accounted for as described below.

i. Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or where appropriate, a shorter period.

Income and expense is recognised on an effective interest basis for debt instruments other than those financial assets designated as at 'fair value through profit or loss' (FVTPL).

ii. Financial Assets

Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned and are initially measured at fair value, plus transaction costs, except for those financial assets classified as FVTPL, which are initially measured at fair value.

Financial assets at the balance sheet date are classified into the following specified categories: financial assets at FVTPL, 'held-to-maturity' investments, 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

iii. Impairment of financial assets

For financial assets carried at amortised cost, the amount of an impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

For financial assets carried at cost less impairment, the impairment loss is the difference between the asset's carrying amount and the best estimate of the amount that would be received for the asset if it were to be sold at the reporting date.

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES - continued

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade debtors.

Where indicators exist for a decrease in impairment loss, and the decrease can be related objectively to an event occurring after the impairment was recognised, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired financial asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised.

iv. Derecognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

v. Trade debtors

Trade debtors are initially recognised at fair value. The carrying amount is reduced through the use of provision. Appropriate provision for estimated irrecoverable amounts are recognised where the estimated cash flows are less than the carrying amount. Subsequent recoveries of amounts previously written off are credited to the profit or loss.

vi. Cash

Cash comprises cash on hand and demand deposits, which are those deposits, which are repayable on demand and available within 24 hours (one day) without penalty.

vii. Short term deposits

Short term deposits comprise of cash deposits that are available with notice of more than 24 hours (one day).

viii. Financial liabilities

Financial liabilities are classified as either financial liabilities at 'FVTPL' or 'other financial liabilities'.

ix. Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- It has been incurred principally for the purpose of disposal in the near future; or
- It is a part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or
- It is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- Such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- The financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy and information about the Company is provided internally on that basis; or
- It forms part of a contract containing one or more embedded derivatives and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES – continued

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

x. Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

xi. De-recognition of financial liabilities

The Company derecognises financial liabilities when, and only when, the Company's obligations are discharged, cancelled or they expire.

xii. Derivative financial instruments and hedge accounting

The Company uses interest rate swaps and foreign exchange forward contracts to hedge interest rate and foreign currency risk arising on debt instruments. On inception of the hedge relationship the Company documents the relationships between the hedged item and the hedging instrument along with the risk management objectives and its strategy for undertaking various transactions. Furthermore, at inception of the hedge and on an ongoing basis the Company documents whether the hedging relationship is highly effective.

Changes in fair value of derivatives that are designated and are effective as hedges of future cash flows are recognised directly in equity within the hedge reserve. The ineffective portion of the hedge is recognised through the profit and loss account.

Changes in the fair value of derivatives that do not qualify for hedge accounting are recognised in the profit and loss account as they arise.

Hedge accounting is discontinued when the hedge instrument expires or is terminated.

Financial assets and financial liabilities are offset where they are settled net as a matter of practice and there is legal right to offset.

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES - continued

Taxation

Current tax, including UK corporation tax and foreign 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 financial statements that arises from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that, 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 measured using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date that are expected to apply to the reversal of the timing difference.

Where items recognised in other comprehensive income or equity are chargeable to or deductible for tax purposes, the resulting current or deferred tax expense or income is presented in the same component of comprehensive income or equity as the transaction or other event that resulted in the tax expense or income.

Current tax assets and liabilities are offset only when there is a legally enforceable right to set off the amounts and the Company intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Deferred tax assets and liabilities are offset only if: a) the Company has a legally enforceable right to set off current tax assets against current tax liabilities; and b) the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Foreign currency

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are reported at the rates of exchange prevailing at that date.

Other exchange differences are recognised in profit or loss in the year in which they arise except for exchange differences on transactions entered into to hedge certain foreign currency risks (see below), and exchange differences arising on gains or losses on non-monetary items which are recognised in other comprehensive income.

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES - continued

Employee benefits

i. Defined benefit pension scheme

The Company participates in a group wide defined benefit pension plan administered by the ultimate parent undertaking, Scotia Gas Networks Limited. The net defined benefit cost of the plan is charged and accounted for based on the proportionate number of members relating to the Company. The contributions payable by the Company is determined on the same basis as the charging policy above.

For defined benefit schemes the amounts charged to operating profit are the costs arising from employee services rendered during the year and the cost of plan introductions, benefit changes, settlements and curtailments. They are included as part of staff costs. The net interest cost on the net defined benefit liability is charged to profit or loss and included within finance costs. Remeasurement comprising actuarial gains and losses and the return on scheme assets (excluding amounts included in net interest on the net defined benefit liability) are recognised immediately in other comprehensive income.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the Company, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit credit method. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date.

When the calculation results in a net asset to the Company, the recognised asset is limited to the present value of any future refunds from the plan or reductions in future contributions to the plan and restricted by any relevant asset ceiling. Any deduction made by the tax authorities in the event of a refund of a surplus would be regarded by the Company as an income tax.

ii. Defined contribution pension scheme

For defined contribution schemes the amount charged to the profit and loss account in respect of pension costs and other retirement benefits is the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. ACCOUNTING POLICIES - continued

Impairment of non-financial assets

Assets, other than those measured at fair value, are assessed for indicators of impairment at each balance sheet date. If there is objective evidence of impairment, an impairment loss is recognised in profit or loss as described below.

An asset is impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition, the estimated recoverable value of the asset has been reduced. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

The recoverable amount of goodwill is derived from measurement of the present value of the future cash flows of the business. Any impairment loss is allocated first to the goodwill, and then to other assets on a pro-rata basis.

Where indicators exist for a decrease in impairment loss, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised. Where a reversal of impairment occurs, the reversal is applied to the assets (other than goodwill) on a pro-rata basis. Goodwill impairment is not reversed.

Borrowing costs capitalised

Borrowing costs which are directly attributable to the construction of qualifying tangible fixed assets are capitalised as part of the cost of those assets. Qualifying tangible fixed assets are considered to be those of significant size or complexity, which typically are under construction for in excess of one year and/or where project costs exceed a pre-determined threshold. The commencement of capitalisation begins when both finance costs and expenditures for the asset are being incurred and activities that are necessary to get the asset ready for use are in progress. Capitalisation ceases when substantially all the activities that are necessary to get the asset ready for use are complete. Borrowing costs are not capitalised in respect of construction projects which do not meet the defined thresholds or relate to replacement expenditure.

Operating leases

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis. Benefits received and receivable as an incentive to sign an operating lease are similarly spread on a straight-line basis over the lease term.

Southern Gas Networks Plc (Registered number: 05167021)

Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

1. **ACCOUNTING POLICIES - continued**

Provisions

A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are discounted where the impact of discounting the expected future cash flows is material.

Interest receivable and Interest payable

Interest payable and similar expenses include interest payable and finance leases recognised in profit or loss using the effective interest method, unwinding of the discount on provisions, and net foreign exchange losses that are recognised in the profit and loss account (see foreign currency accounting policy).

Other interest receivable and similar income include interest receivable on funds invested and net foreign exchange gains.

Interest income and interest payable are recognised in profit or loss as they accrue, using the effective interest method. Dividend income is recognised in the profit and loss account on the date the entity's right to receive payments is established. Foreign currency gains and losses are reported on a net basis.

Dividends

Equity dividends are recognised when they become legally payable. Interim equity dividends are recognised when paid. Final equity dividends are recognised when approved by the shareholders at an annual general meeting.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY**

In the application of the Company's accounting policies, which are described in note 1, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

Critical accounting judgements

- a. Cost classification - the allocation of overhead costs to capital investment projects is subject to accounting judgement, particularly around the amount of time spent on different activities. Guidelines have been established, and a Cost Allocation Model is used as part of a process to determine the split of attributable overheads between capital expenditure and operating expenditure.
- b. Impairment of fixed assets - as set out in note 1 above, management has exercised judgement during the company balance sheet review when identifying impairment indicators affecting the legacy gas meter portfolio of the Company and when determining an appropriate revised useful economic life for these assets.

Key source of estimation uncertainty

- a. Useful lives of assets - The Group depreciates its assets over their useful economic lives. The estimation of the useful lives of assets is based on historic performance as well as expectations about future use and therefore requires estimates and assumptions to be applied by management. The useful economic lives of assets can vary depending on a variety of factors, including technological innovation, product life cycles, maintenance programmes as well as the economic life of the gas industry. The depreciation policy is set out in note 1.
- b. Retirement benefit schemes - the assumptions used in accounting for the defined benefit pension scheme are based on estimates and are subject to uncertainties. These assumptions are set out in the employee benefit obligations note and include: the discount rate on scheme liabilities, mortality rates, pension increases, salary increases and inflation. The Company takes advice from independent actuaries on the appropriateness of these assumptions
- c. Valuation of financial instruments - where financial instruments are recognised at fair value there are uncertainties in forward yield curves used in discounted cash flow calculations.
- d. Environmental provision - in assessing the degree of contamination at the various sites estimation is required where elements of the contamination are underground. In these cases, it is difficult to assess with any certainty the extent of the contamination. The discount rate is also a source of estimation.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**3. EMPLOYEES AND DIRECTORS**

The Company had 470 full time equivalent employees as at 31 March 2021 (2020: 506). The average monthly number of full time equivalent employees during the year was 480 (2020: 528).

	2021	2020
Field based staff	227	247
Office and other administrative staff	243	259
	<u>470</u>	<u>506</u>

The Independent Directors received remuneration totalling £62,953 (2020: £48,925) for their services to the Company during the year. No retirement benefits are accruing in the year or in the prior year to any Directors under money purchase or defined benefit schemes, in respect of their services to the Company. There are 8 directors who did not receive any remuneration in respect of services to the company during the current or preceding financial year. These directors are employed by the SGN Group's shareholders and do not specifically receive any remuneration in respect of the company.

Staff costs for the Company during the year are as follows:

	2021 £m	2020 £m
Wages and salaries	24	24
Social security costs	3	4
Pension costs (Note 23)	17	18
	<u>44</u>	<u>46</u>

4. INTEREST RECEIVABLE AND SIMILAR INCOME

	2021 £m	2020 £m
Net defined benefit pension income	<u>5</u>	<u>3</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**5. INTEREST PAYABLE AND SIMILAR EXPENSES**

	2021 £m	2020 £m
Movement in financial derivatives	2	-
Other interest payable on bonds	91	93
Index linked bond interest	14	23
Unwind of discount	-	1
	<u>107</u>	<u>117</u>

During the year, the Company incurred borrowing costs of £2.2m which were included in the carrying amount of the issued bond (2020: £nil).

6. PROFIT BEFORE TAXATION

The profit is stated after charging/(crediting):

	2021 £m	2020 as restated £m
Depreciation - owned assets	116	113
Loss on disposal of fixed assets	5	5
Goodwill amortisation	6	5
Computer software amortisation	7	9
Amortisation of customer contributions	(6)	(6)
Operating lease rentals	<u>3</u>	<u>3</u>

Auditor's remuneration for the Company comprises:

- Audit of these financial statements £127,500 (2020: £116,600)
- Audit-related assurance services £40,000 (2020: £42,950)
- Other assurance services £18,000 (2020: £12,360)

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**7. TAXATION****Analysis of the tax charge**

The tax charge on the profit for the year was as follows:

	2021	2020 as restated
	£m	£m
Current tax:		
UK corporation tax	56	59
Prior period adjustment	<u>(1)</u>	<u>(3)</u>
Total current tax	<u>55</u>	<u>56</u>
Deferred tax:		
Origination and reversal of timing differences	(9)	(8)
Prior period adjustment	1	2
Effect of change in tax rate	<u>-</u>	<u>61</u>
Total deferred tax	<u>(8)</u>	<u>55</u>
Tax on profit	<u><u>47</u></u>	<u><u>111</u></u>

UK corporation tax has been charged at 19% (2020 - 19%).

Reconciliation of total tax charge included in profit and loss

The tax assessed for the year is higher than (2020: higher than) the standard rate of corporation tax in the UK. The difference is explained below:

	2021	2020 as restated
	£m	£m
Profit before tax	<u>243</u>	<u>259</u>
Profit multiplied by the standard rate of corporation tax in the UK of 19% (2020 - 19%)	46	49
Effects of:		
Non-deductible goodwill	1	1
Effect of change in tax rates	<u>-</u>	<u>61</u>
Total tax charge	<u><u>47</u></u>	<u><u>111</u></u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**7. TAXATION - continued****Tax effects relating to effects of other comprehensive income**

		2021	
	Gross	Tax	Net
	£m	£m	£m
(Loss)/Gain arising on cash flow hedges	(1)	-	(1)
Remeasurement on net pension asset	(41)	8	(33)
	<u>(42)</u>	<u>8</u>	<u>(34)</u>

		2020	
	Gross	Tax	Net
	£m	£m	£m
Gains arising on cash flow hedges	1	-	1
Remeasurement net defined benefit asset	82	(16)	66
	<u>83</u>	<u>(16)</u>	<u>67</u>

The standard rate of tax applied to reported profit on ordinary activities is 19% (2020: 19%). Finance Bill 2016 reduced the main rate of corporation tax from 19% to 17% from 1 April 2020. Finance Bill 2020 has amended the main rate of corporation tax to remain at 19% from 1 April 2020 and 1 April 2021. As these changes have been substantively enacted at the balance sheet date deferred tax has been calculated accordingly and this has had the effect of increasing the company's deferred tax liability at 31 March 2021 by £nil (2020: £60.5m).

There is no expiry date on timing differences, unused tax losses or tax credits.

For the purposes of FRS 102, the Finance Bill 2021 has been substantively enacted on 24 May 2021. The Finance Bill 2021 will increase the main corporation tax rate from 1 April 2023 from 19% to 25%. The Company's deferred tax liability is estimated to increase by £182m to £759m due to this change in tax rate.

8. DIVIDENDS

Dividends paid for the year ended 31 March 2021 amount to £81m (50.32p per share) (2020: £53m (33.90p per share)). No further dividends were proposed.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**9. PRIOR YEAR ADJUSTMENT****Prior year adjustments****a.) Legacy gas meters**

During the year, a company balance sheet review identified two errors relating to legacy metering assets (part of plant and machinery) which were found to have been in existence in previous reporting periods:

1) impairment indicators were noted in relation to the Company's meter asset portfolio which would have resulted in an impairment charge in prior years.

The key impairment indicators observed:

- technological obsolescence (i.e. the emergence of smart meters)
- the UK government's smart meter rollout programme which aims to replace all existing gas meters with smart meters by 2025
- reduction in revenue from gas meters as they become out of use
- an increase in early termination charge on meters that are discontinued earlier than it was contractually agreed

2) The existence of legacy meter assets included on the fixed asset register which had previously been removed from service resulting in a write off which should have been recorded in prior years.

As both of these errors were:

- (a) in existence in previous reporting periods when the financial statements for those periods were authorised for issue and
- (b) could reasonably be expected to have been taken into consideration when preparing those financial statements, a prior period adjustment is required in the financial statements as 31 March 2021.

The errors have been corrected by restating each of the affected financial statement line items for the prior periods, as follows:

Impact on equity

	31 March 2020	1 April 2019
	£m	£m
Fixed assets	0.5	(4.7)
Total assets	0.5	(4.7)
Deferred tax	(0.1)	0.9
Total liabilities	(0.1)	0.9
Net impact on equity (increase/(decrease) in equity)	0.4	(3.8)

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**Impact on statement of profit or loss**

	31 March 2020
	£m
Depreciation	(0.5)
Tax impact of the change in depreciation	<u>0.1</u>
Increase in profit for the year	<u><u>(0.4)</u></u>

The £4.7m impact to fixed assets as at 1 April 2019 reflects the write off and impairment of the legacy assets. The £0.5m impact to fixed assets is to add back the over depreciation in the year ended 31 March 2020.

Consequently, the useful life of the remaining meter assets were revised.

10. INTANGIBLE FIXED ASSETS

	Goodwill £m	Computer software £m	Totals £m
COST			
At 1 April 2020	288	114	402
Additions	<u>-</u>	<u>3</u>	<u>3</u>
At 31 March 2021	<u>288</u>	<u>117</u>	<u>405</u>
AMORTISATION			
At 1 April 2020	85	87	172
Amortisation for year	<u>6</u>	<u>7</u>	<u>13</u>
At 31 March 2021	<u>91</u>	<u>94</u>	<u>185</u>
NET BOOK VALUE			
At 31 March 2021	<u>197</u>	<u>23</u>	<u>220</u>
At 31 March 2020	<u>203</u>	<u>27</u>	<u>230</u>

There is no security held against the intangible fixed assets of the Company.

The amortisation charge is recognised in operating costs in the profit and loss account.

The goodwill, which arose on the acquisitions of the business by the Company is being amortised on a straight-line basis over 50 years, with 34 years remaining. 50 years is the expected life of the network and is consistent with the long-term outlook of the Regulator.

A review for impairment of goodwill is carried out when there are indicators of impairment. Impairment testing is performed by comparing the carrying value of fixed assets at the balance sheet date with the recoverable amount. The recoverable amount is the higher of the value if sold or its value in use.

No impairment loss has been recorded in the current year or prior years.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**11. TANGIBLE FIXED ASSETS**

	Freehold property £m	Plant and machinery £m	Computer equipment £m	Total £m
COST				
At 1 April 2020 (restated)	83	5,551	65	5,699
Additions	6	250	6	262
Disposals		(8)	(2)	(10)
	<u>89</u>	<u>5,793</u>	<u>69</u>	<u>5,951</u>
At 31 March 2021				
	<u>89</u>	<u>5,793</u>	<u>69</u>	<u>5,951</u>
DEPRECIATION				
At 1 April 2020 (restated)	30	1,031	36	1,097
Charge for the year	3	107	6	116
Eliminated on disposal		(4)	(1)	(5)
	<u>33</u>	<u>1,134</u>	<u>41</u>	<u>1,208</u>
At 31 March 2021				
	<u>33</u>	<u>1,134</u>	<u>41</u>	<u>1,208</u>
NET BOOK VALUE				
At 31 March 2021	<u>56</u>	<u>4,659</u>	<u>28</u>	<u>4,743</u>
At 31 March 2020 (restated)	<u>53</u>	<u>4,520</u>	<u>29</u>	<u>4,602</u>

Customer contributions

The Company has received customer contributions relating to plant and machinery. In accordance with the Company's accounting policy the assets are capitalised within fixed assets and the contributions are recognised as deferred income in the balance sheet. The connections contributions are from customers being connected to the network and replacement contributions are related to the diversion of gas mains. The deferred income is released to the profit and loss account over the estimated lives of the related assets. The amount deferred under this policy was as follows:

	Connections 2021 £m	Replacement 2021 £m	Total 2021 £m
Customer contributions brought forward	156	88	244
Customer contributions deferred in the year	10	15	25
Amortisation in year	<u>(4)</u>	<u>(2)</u>	<u>(6)</u>
	<u>162</u>	<u>101</u>	<u>263</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**12. DEBTORS: AMOUNTS FALLING DUE WITHIN ONE YEAR**

	2021	2020
	£m	£m
Trade debtors	62	69
Other debtors	1	-
Tax	2	-
Prepayments and accrued income	9	7
	<u>74</u>	<u>76</u>

13. SHORT TERM DEPOSITS

	2021	2020
	£m	£m
Short term deposits	<u>97</u>	<u>82</u>

14. CASH AT BANK

	2021	2020
	£m	£m
Cash at bank	<u>2</u>	<u>3</u>

15. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2021	2020
	£m	£m
Borrowings (see note 17)	-	215
Trade creditors	23	25
Amounts owed to group undertakings	42	57
Social security and other taxes	19	17
Other creditors	7	10
Other accrued interest	34	37
Deferred income	29	24
Accruals	75	68
	<u>229</u>	<u>453</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**15. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR - continued**

Amounts owed to group undertakings includes an intercompany loan due to Scotland Gas Networks plc of £45m (2020: £62m) and to SGN Natural Gas Ltd of £7m (2020: £5m). Both loans are repayable on demand and both bear interest at the Bank of England Base Rate.

Also included are intercompany trade balances due from the Group of £10m (2020: £9m).

Included in borrowings falling due within one year, are loans and public bonds consisting of:

	2021 £m	2020 £
£215m 4.875% fixed rate note due 2020	-	215
	-	215

The total revolving credit facility is £240m (2020: £340m) and expires in March 2025. The facility was undrawn at 31 March 2021 (2020: undrawn).

16. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	2021 £m	2020 £m
Borrowings (see note 17)	2,951	2,698
Derivative financial liabilities - mirror swaps	21	26
	<u>2,972</u>	<u>2,724</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**16. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR - continued**

Included in borrowings falling due after more than one year, are public bonds, private placement notes and loans consisting of:

	2021 £m	2020 £m
Fixed rate:		
£300m 4.875% fixed rate note due 2023 [1]	299	299
£350m 2.5% fixed rate note due 2025 [1]	348	348
£375m 4.875% fixed rate note due 2029 [1]	374	374
£75m 2.74% fixed rate note due 2030	75	75
£75m 2.87% fixed rate note due 2033	75	75
£250m 1.250% fixed rate note due 2031 [1]	248	-
£100m 2.27% fixed rate note due 2034	100	100
£400m 3.1% fixed rate note due 2036 [1]	398	398
£225m 6.375% fixed rate note due 2040 [1]	224	224
	<u>2,141</u>	<u>1,893</u>
Index-linked:		
£150m 2.066% index-linked note due 2025 [1]	232	230
£83.3m 2.013% index-linked note due 2025 [1]	128	127
£15m 2.580% index-linked loan due 2028	21	21
£83.3m 2.013% index-linked note due 2035 [1]	129	127
	<u>510</u>	<u>505</u>
Floating rate:		
£125m floating rate note due 2025	125	125
£80m floating rate note due 2026	80	80
£60m floating rate loan note due 2026	60	60
£35m floating rate loan note due 2026	35	35
	<u>300</u>	<u>300</u>
Total borrowings	<u><u>2,951</u></u>	<u><u>2,698</u></u>

[1] listed on the London Stock Exchange.

The above borrowings are unsecured and are stated after the deduction of unamortised issue costs of £9m (2020: £8m). These costs together with the interest expense are allocated to the profit and loss account over the term of the borrowings. Interest is calculated using the effective interest rate method.

Certain interest costs in respect of index-linked bonds are not payable until the principal amount of the bond is repaid and are included within the carrying value of the borrowings stated above. The amount included in the carrying value of the borrowings at 31 March 2021 is £179m (2020: £175m). The amount debited to the profit and loss account in relation to accretion during the year amounted to £4m (2020: £13m).

The total revolving credit facility is £240m (2020: £340m) and expires in March 2025. The facility is undrawn at the year end.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**16. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR - continued**

Included within creditors falling due after more than one year are derivatives at fair value through profit and loss with a net fair value of £21m (2020: £26m), which are subject to net settlement provisions with a single counterparty. This portfolio comprises long dated pay fixed/receive floating interest rate swaps originally taken out in 2005-06 to fix the Company's interest cost over periods out to 2025, together with pay floating/receive fixed swaps taken out at a later date within the financial year. The cash flow payment dates and floating leg payment terms match off, although the fixed interest payable on the offsetting swaps is in excess of the original swaps. Changes in the fair value of the portfolio on a net basis are recognised in the profit and loss account as they arise.

Mirror swaps

In 2005 the Company entered into interest rate swap contracts to fix the Company's interest cost relating to (floating rate) bridging loans which were in place at the time. In October 2005, permanent long-term capital markets debt was issued to replace floating rate bridging loans. At that point these swaps became obsolete and consequently matching swaps were transacted (under which the Group received fixed rate interest) to close out the position. The crystallised loss was recognised in the profit and loss and a discounted balance equal to the market value of the matched swaps was established within creditors. At 31 March 2021 the mirror swap loss was £21m (2020: £26m).

17. BORROWINGS

An analysis of the maturity of public bonds, private placement notes and loans is given below:

	2021	2020
	£m	£m
Between one and five years	1,213	647
After five years	<u>1,738</u>	<u>2,051</u>
	2,951	2,698
On demand or within one year	<u>-</u>	<u>215</u>
	<u><u>2,951</u></u>	<u><u>2,913</u></u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**18. FINANCIAL INSTRUMENTS**

The Company's funding, liquidity and exposure to interest rate, foreign currency exchange and credit risks are managed within a framework of policies and guidelines authorised by the Board of Directors. In accordance with these policies, and in accordance with covenants set out as part of bond issuances made by the Company, financial derivatives are used to manage financial exposures.

The Company is a wholly owned subsidiary of SGN MidCo Limited and accordingly is, under FRS 102 exempt from certain disclosures required under sections 11 and 12 as these are detailed in the annual report of Scotia Gas Networks Limited.

Movement in derivatives included in profit and loss account

The net movement included within interest in the profit and loss account for financial derivatives is £1m (2020: nil)

In addition, the movement on mirror swaps in the year was a loss of £1m (2020: £1m) included in interest payable.

Categories of financial instrument

The categories of financial liabilities held by the company are as follows:

	2021	2020
	£m	£m
Financial liabilities held at amortised cost		
Trade creditors	23	26
Accrued interest	34	37
Accruals	75	68
Borrowings	<u>2,951</u>	<u>2,913</u>
	3,083	3,044
Financial liabilities held at fair value		
Financial derivatives - mirror swaps	<u>21</u>	<u>26</u>
	<u>21</u>	<u>26</u>
Total financial liabilities	<u>3,104</u>	<u>3,070</u>

The financial liabilities held at fair value are stated after credit risk adjustments of £nil (2020: £0.9m).

19. PROVISIONS FOR LIABILITIES

	2021	2020
	£m	as restated £m
Deferred tax	<u>577</u>	<u>593</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

	2021	2020 as restated
	£m	£m
Other provisions		
Other provisions	9	7
Environmental provisions	<u>6</u>	<u>7</u>
	<u>15</u>	<u>14</u>
 Aggregate amounts	 <u>592</u>	 <u>607</u>
	Deferred tax	Other provisions
	£m	£m
Balance at 1 April 2020		
As previously reported	594	14
Prior year adjustment	<u>(1)</u>	-
As restated	593	14
Provided during year	-	2
Net movement in deferred tax	(16)	-
Reassessment during the year	<u>-</u>	<u>(1)</u>
Balance at 31 March 2021	<u>577</u>	<u>15</u>

Environmental

The environmental provision represents the Directors' best estimate of environmental restoration costs, where the Company has a legal obligation to restore sites at the balance sheet date. The provision has been discounted and is stated at the present value of the expenditure expected to be required to settle the obligation. The provision is expected to be utilised over the next five years in line with anticipated regulatory outputs requirements for land remediation.

Other provisions

Other provisions include asbestos related liabilities. The provision has been discounted and is stated at the present value of the estimated expenditure to settle the obligation. The provision is expected to be utilised over the next 30 years.

Deferred tax

Deferred tax is provided as follows:

	2021	Restated 2020
	£m	£m
Accelerated capital allowances	542	552
Deferred tax on retirement benefit obligations	<u>35</u>	<u>41</u>
Deferred tax	<u>577</u>	<u>593</u>

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**19. PROVISIONS FOR LIABILITIES - continued**

The movement in provision for deferred tax is as follows:

	2021	Restated 2020
	£m	£m
Opening balance	593	523
(Credited)/charged to profit and loss account	(8)	54
Movement through other comprehensive income	(8)	16
	<u>577</u>	<u>593</u>
Deferred tax	<u>577</u>	<u>593</u>

The Company is not expecting a reversal of deferred tax in the next financial year. Overall deferred tax is expected to increase due to the changes in tax rates now enacted. For further information refer to note 26.

There is no expiry date on timing differences, unused tax losses or tax credits.

Deferred tax has been measured based upon corporation tax rates substantively enacted at the balance sheet date. (Information regarding rates of corporation tax can be found in taxation note in notes to the financial statements.)

Deferred tax assets and liabilities are offset only where the Company has a legally enforceable right to do so and where the assets and liabilities relate to income taxes levied by the same taxation authority on the same taxable entity or another entity within the Company.

The Company has no unrecognised deferred tax assets or liabilities.

20. DEFERRED INCOME

	2021	2020
	£m	£m
Deferred income (Note 11)	<u>263</u>	<u>244</u>

21. CALLED UP SHARE CAPITAL

Allotted, issued and fully paid:

Number:	Class:	Nominal value:	2021	2020
			£	£
160,174,772	Ordinary	£1	<u>160,174,772</u>	<u>160,174,772</u>

There is a single class of ordinary shares. There are no restrictions on the distribution of the dividends and the repayment of capital.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**22. RESERVES**

	Profit and loss account £m	Hedging reserves £m	Totals £m
At 1 April 2020	1,017	1	1,018
Profit for the year	196	-	196
Dividends	(81)	-	(81)
Movement in cash flow hedges	-	(1)	(1)
Defined benefit pension asset	<u>(33)</u>	<u>-</u>	<u>(33)</u>
At 31 March 2021	<u>1,099</u>	<u>-</u>	<u>1,099</u>

The hedging reserve represents the cumulative portion of gains and losses on hedging instruments deemed effective in hedging variable interest rate risk of recognised financial instruments or foreign exchange risk in firm commitments or highly probable forecast transactions. Amounts accumulated in this reserve are reclassified to profit or loss in the periods in which the hedged item affects profit or loss or when the hedging relationship ends.

23. EMPLOYEE BENEFIT OBLIGATIONS**Defined contribution schemes**

The Company operates a defined contribution retirement benefit schemes for all qualifying employees of the Group.

The amount recognised in the profit and loss account is as follows:

	2021 £m	2020 £m
Amount charged in respect of defined contribution schemes	<u>8</u>	<u>7</u>

At the balance sheet date, there were outstanding contributions of £nil (2020: £nil).

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**Defined benefit schemes**

The Company is a wholly owned subsidiary of SGN MidCo Limited. The ultimate parent undertaking is Scotia Gas Networks which operates the Scotia Gas Networks Pension Scheme, a defined benefit scheme for a significant number of its employees of its subsidiaries who prior to 1 December 2005 were previously members of the Lattice Company Scheme and had joined prior to 31 March 2002. Under the Scheme, the employees are entitled to retirement benefits based on final salary on attainment of retirement age (or earlier withdrawal or death). The Scheme is open to future accrual of benefits and closed to new members. Employees joining the Lattice Company Scheme after 31 March 2002 were entitled to join a defined contribution scheme. Under the Group cost allocation plan, the Company accounts for its agreed share of the total net defined benefit cost, based on the proportionate members relating to the Company.

The most recent triennial valuation of the Scheme was carried out at 31 March 2018. The Company has employed an independent actuary to approximately update this valuation allowing for differences between the actuarial assumptions used by the Scheme for funding purposes and those adopted by the Company to measure the Scheme's liabilities on the financial statements, as well as adjusting for benefit accrual and benefits paid by the Scheme. The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method. In accordance with FRS 102, a limited actuarial review has been carried out by PwC at 31 March 2021 using the projected unit method.

	As at 31 March 20 21	As at 31 March 20 20
Key assumptions used:		
Retail price inflation	3.5% p.a.	2.8% p.a.
Consumer price inflation	3.1% p.a.	1.8% p.a.
Rate of increase of pensions payment	3.5% p.a.	2.8% p.a.
Rate of increase of salaries	3.3% p.a.	2.6% p.a.
Discount rate	<u>2.0% p.a.</u>	<u>2.3% p.a.</u>

The discount rate is based on the return of high quality corporate bonds.

The assumptions relating to longevity underlying the pension liabilities reflect the characteristics of the Scheme membership ('VitaCurves') for base mortality, with an allowance for further improvements in life expectancy in line with the medium cohort adjustments subject to a 1.5% p.a. underpin in the longevity assumption. The assumed life expectations on retirement at age 65 are:

As at 31 March	2021		2020		2019	
	Male	Female	Male	Female	Male	Female
Members currently aged 65	22.7	24.3	22.7	24.2	22.4	23.9
Members currently aged 45	24.4	26.9	24.3	26.4	24.2	26.5

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

The approximate effects of movements in the main assumptions on the defined benefit obligation are shown in the table below:

	Sensitivity	Approximate change in DBO £000
Discount rate	- 0.1% p.a. + 0.1% p.a.	11,483 (11,168)
Price inflation (RPI measure)*	- 0.1% p.a. + 0.1% p.a.	(10,529) 10,768
Life expectancy	- 1 year + 1 year	(21,766) 22,786

*These movements have been calculated assuming that changes in the inflation assumption have a knock-on effect on the pension increase and salary growth assumptions (i.e. the "real" increase rates are maintained). Note that the sensitivities do not allow for the movement in the insured pensioner asset, therefore the net balance sheet movement is smaller.

The analysis of scheme assets and the amount included in the balance sheet arising from the Company's obligations in respect of its defined benefit retirement benefit schemes at the balance sheet date is as follows:

As at 31 March	2021			2020		
			Total	Unquoted		Total
	Quoted	Unquoted		Quoted	Unquoted	
	Fair Value	Fair Value	Fair Value	Fair Value	Fair Value	Fair Value
	£m	£m	£m	£m	£m	£m
Equities	81	-	81	67	-	67
Government bonds [2]	277	-	277	372	-	372
Corporate bonds	125	84	209	110	81	191
Property	-	-	-	1	-	1
Cash	12	-	12	5	-	5
Insurance contracts	-	162	162	-	47	47
Total market value of assets	495	246	741	555	128	683
Actuarial value of liabilities			(562)			(470)
Net pension asset			179			213

[2] Including LDI repurchase agreement liabilities.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

The fair value of scheme assets at 31 March 2021 are based on the bid price where available. The fair value of property is based on the mid price and the value of the single unit price funds is based on the single unit price.

To reduce the risk of volatility in the Scheme's funding level, a liability driven investment (LDI) strategy forms part of the assets employed within the investment strategy of the Scheme. The LDI strategy provides c95% interest rate protection and c95% inflation protection as at 31 March 2021 with respect to the pension scheme liabilities of c.£0.6bn (valued using a UK government bond yield curve). The Scheme assets which provide this interest rate and inflation protection are managed by BlackRock and Goldman Sachs and include a variety of instruments e.g. UK government bonds (gilts), interest rate swaps, inflation swaps, gilt repos and corporate bonds. The Scheme has implemented a pensioner buy in which also contributes to the total interest rate and protection ratios referred to above.

Movements in the present value of defined benefit obligations were as follows:

	2021 £m	2020 £m
At 1 April	(470)	(548)
Current service cost	(9)	(11)
Administration costs	-	(1)
Interest cost	(11)	(12)
Actuarial (losses)/gains	(96)	78
Benefits paid	24	24
	<hr/>	<hr/>
At 31 March	(562)	(470)

Movement in the fair value of scheme assets were as follows:

	2021 £m	2020 £m
At 1 April	683	668
Interest income	16	15
Contributions from the Company	12	20
Remeasurement of scheme assets	55	4
Benefits paid	(24)	(24)
Administration costs	(1)	-
	<hr/>	<hr/>
As at 31 March	741	683

The actual gain on scheme assets was £59m (2020: £19m).

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

Employer contributions for the period ending 31 March 2021 were 37.3% (2020: 37.3%) of monthly salary roll, before allowing for any salary sacrifice contributions. Deficit contributions are also payable at the rate of £7.5m p.a. from 1 April 2020 to 31 March 2027 (2020: £14.1m p.a. less 2.7% of salary roll (with the annual salary roll calculated in March each year and used for the following 12 months beginning 1 April)).

Amounts recognised in the profit and loss account in respect of these defined benefit schemes are as follows:

	2021 £m	2020 £m
Current service cost	(9)	(11)
Administration costs	(1)	(1)
Total charged to operating profit:	(10)	(12)
Expected return on scheme assets	16	15
Interest charge on scheme liabilities	(11)	(12)
Net interest credit	5	3
Total charge to the profit and loss account	(5)	(9)

	2021 £m	2020 £m
Actuarial gains on scheme assets	55	4
Actuarial (losses)/gains on scheme obligations	(96)	78
(Losses)/gains recognised in other comprehensive income	(41)	82

24. FINANCIAL COMMITMENTS

Capital projects contracted for by the Company but not provided in the financial information amounted to £11m at 31 March 2021 (2020: £28m). Within this amount £1m (2020: £6m) is related to intangible assets.

Total future minimum lease payments under non-cancellable operating leases for the Company are as follows:

	Other		Land and Buildings	
	2021 £m	2020 £m	2021 £m	2020 £m
- less than one year	2	2	1	1
- between two to five years	2	2	2	2
- after five years	-	-	13	11

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021**25. RELATED PARTY DISCLOSURES**

The Company is a subsidiary undertaking of SGN MidCo Limited. The ultimate controlling party of the Company is Scotia Gas Networks Limited, a Company registered in England and Wales.

The largest group in which the results of the Company are consolidated is that headed by Scotia Gas Networks Limited, St Lawrence House, Station Approach, Horley, Surrey RH6 9HJ, United Kingdom. The smallest group in which they are consolidated is that headed by SGN MidCo Limited, St Lawrence House, Station Approach, Horley, Surrey RH6 9HJ, United Kingdom. Copies of Scotia Gas Networks Limited consolidated financial statements can be obtained from the Company Secretary, St Lawrence House, Station Approach, Horley, Surrey RH6 9HJ, United Kingdom.

Scotia Gas Networks Limited is owned by a consortium consisting of SSE plc (33%), Borealis Infrastructure Europe (UK) Limited (25%) which is indirectly wholly owned by OMERS Administration Corporation, OTPPB Investments (UK) Limited (25%), which is owned by Ontario Teachers' Pension Plan Board, and Blue Spyder B 2016 Limited (17%), which is owned by Abu Dhabi Investment Authority. It is the opinion of the Directors that the parent Company, Scotia Gas Networks Limited, has no single controlling party as that Company is controlled jointly by the consortium.

In accordance with FRS102 the Company is exempt from disclosing transactions with subsidiaries that are wholly owned by the group.

As at 31 March 2021 amounts owed to group undertakings includes an intercompany loan due to Scotland Gas Networks plc of £45m (2020: £62m) and to SGN Natural Gas Ltd of £7m (2020: £5m). Both loans are repayable on demand and both bear interest at the Bank of England Base Rate. Also included are intercompany trade balances due from the Group of £10m (2020: £9m).

Transactions with Key Management Personnel

The Company's ultimate parent undertaking, Scotia Gas Networks includes the Company in its consolidated financial statements. In these financial statements, the Company is considered to be a qualifying entity and has applied the exemptions available under FRS 102 in respect of the Key Management Personnel compensation disclosures.

Transactions with shareholders

Amounts owed to shareholders and loans from shareholders are set out below:

	2021 £m	2020 £m
Other amounts owed to shareholders:		
SSE plc	<u>10</u>	<u>10</u>

The amounts owed to shareholders mainly comprise amounts payable in respect of a managed service agreement for corporate services and material purchases.

Southern Gas Networks Plc (Registered number: 05167021)Notes to the Financial Statements - continued
for the Year Ended 31 March 2021

The following transactions took place during the year between the Company and the SSE plc group of companies ("SSE").

	2021	2020
	£m	£m
Sales of goods and services	8	69
Purchase of goods and services	(21)	(26)

Sales of goods and services to SSE primarily represent gas transportation services. At 31 March 2021 an amount of £nil was owed by SSE in relation to these services.

SSE provides services to the Company in the form of a management services agreement for corporate services. The Company also purchases certain items such as consumables stock, shrinkage gas and public liability insurance from SSE.

26. **SUBSEQUENT EVENTS**

For the purposes of FRS 102, the Finance Bill 2021 has been substantively enacted on 24 May 2021. The Finance Bill 2021 will increase the main corporation tax rate from 1 April 2023 from 19% to 25%.

The Company's deferred tax liability is estimated to increase by £182m to £759m due to this change in tax rate.