SGN
Your gas. Our network.

Annual Report and Financial Statements 2023

An authentic leader in customer care

Our team is focused on giving our customers a great experience

SGN in numbers

Live document links

This Annual Report is available as an online pdf only and not printed. We have therefore included live links on the contents list and primary accounting statements (to aid navigation) and elsewhere throughout the document (to signpost extra related information elsewhere).

Contents

Our 2022/23 Annual Report brings together the key elements of the year. It incorporates a wide-ranging overview of the Company, statement from the Chair and an introduction from the CEO.

The Strategic Report section contains our operational review for the year, plus the financial review along with our ESG report and the new TCFD report.

The Governance section sets out the governance structures in place, lists the Board of Directors, the make-up of the Board committees and the Board activities.

The final section contains all the financial statements and accounts relevant to the year.

Network investment in 2022/23

£409.4m

17.4% increase on 2021/22

Turnover in 2022/23

£1,288.5m

15.5% increase on 2021/22

Cash flow after investing activities[1] in 2022/23

£299.5m

46.2% increase on 2021/22

Regulatory Asset Value as at 31 March 2023

£6.97bn

9.2% increase on 2021/22

Vulnerable households offered assistance or advice in 2022/23

118,731

127.7% increase on 2021/22

Total carbon footprint in 2022/23

747,795 tCO_2e

2.3% decrease on 2021/22

2022/23 network gas mains replacement

831km

2.1% decrease on 2021/22

External awards in 2022/23

10

[1] Defined in Alternative Performance Measures (APMs) on page 125.

Chair’s statement

This year has been one of change, renewed focus and challenge.

We were delighted to welcome Mark Wild OBE as our new CEO. Mark joined SGN from Crossrail where he led the successful completion of the Elizabeth Line. I believe Mark is an outstanding leader who will steer SGN to achieve ever higher levels of performance for the benefit of all stakeholders.

We also said goodbye to John Morea who retired as CEO after 17 years leading the organisation. We thank him for all his achievements and wish him well.

For all of us at SGN, last August will be remembered for an explosion in Galpin’s Road, south London, which tragically claimed the life of a young girl and left several people with injuries.

Our thoughts remain with the family and everyone in the local community who have been affected by this terrible event. We are continuing to support the ongoing investigation by the Metropolitan Police and Health and Safety Executive.

Looking after our vulnerable customers

SGN performs an essential round-the-clock service for our communities to keep millions of customers safe and warm. So as Russia’s war in Ukraine sent energy prices higher and soaring inflation hit household budgets, we stepped in to provide even more support. We developed more than 40 initiatives, working with a comprehensive array of national and local partners to identify the most vulnerable and help them keep warm.

It was also encouraging to see both our Scottish and Southern networks scoring more than 9/10 for annual customer satisfaction with Scotland maintaining number 1 status for the seventh year running. I am pleased to say that our efforts were recognised with several industry awards for customer service.

Increasing our resources

While overall customer satisfaction remained high, it was a difficult winter. An intense cold snap pre-Christmas led to an unprecedented surge in calls to the national 0800 number for reporting gas escapes. As a result, along with other contributing factors and despite our best efforts across our Scotland and Southern network areas, we did not achieve all our regulatory standards for responding to gas escapes.

We take this responsibility extremely seriously and are taking immediate action to increase our resources and improve our processes for next winter and beyond.

I would like to voice my profound thanks to the entire workforce for their hard work and commitment during this challenging period.

Shaping the UK’s energy future

Our vision is to give our customers the best clean energy experience. To meet the challenge of net zero, people and businesses will need to act differently to make sure everyone has secure, affordable and sustainable energy. We believe this is an exciting opportunity requiring radically innovative solutions.

Our long-term stewardship of critical national infrastructure and a highly skilled workforce puts the Company in a strong position to support the development of the UK’s hydrogen economy. As a leader in whole systems thinking, SGN will champion an integrated energy mix that works for customer and country.

We believe hydrogen and biomethane can play a key role in decarbonising gas networks. They also offer a choice to millions of consumers who will not want to be forced along a particular path when it comes to heating their homes.

That is why we are developing pioneering clean energy projects to help the UK meet its net-zero targets, such as our world-first H100 project in Fife (see page 14). Our market-leading experience in biomethane will also be crucial.

Backed by investors, customers and policymakers across the UK, the hydrogen sector is making great progress and has a very bright future.

With a new CEO in Mark Wild and a growing workforce, we have renewed focus. I am excited about the future of SGN and the key role we play in serving our communities by keeping everyone safe and warm while helping our customers navigate the energy transition in the years ahead.

Nick Salmon
Chair
27 July 2023

Introduction from the Chief Executive

It is an inspiring and challenging time to work in the energy sector.

The gas networks play a crucial role in the communities they serve and through our obligation to help the UK transition to net zero.

In my first few months with SGN, I have been impressed by the dedication of our people, especially our engineers on the frontline.

I joined SGN at a time of great sadness, days after an explosion in Galpin's Road, south London, which resulted in a fatality and injuries to others.

Everyone affected by this tragic incident naturally remains in our thoughts. The cause of the explosion is subject to an ongoing investigation by the authorities which SGN is continuing to support.

A challenging time

Across the UK, it has been a difficult time for many, particularly during the winter. Our teams have been working night and day to look after millions of customers across our networks.

Against this backdrop, safety is our most important priority – for our people and our customers. We want SGN to be a zero-harm business. Our safety record is good but we are committed to making it great.

Preparing for the future

We are committed to building a thriving and enduring SGN. To do that we need to modernise and resource the business to maintain high standards today, preparing ourselves to help shape the UK's energy future.

As a key part of the UK's critical national infrastructure, we are also taking action to make sure our cyber security capability continues to be fit for purpose.

SGN is a regulated business, subject to regular price controls. This year we have stepped up preparations for the next one (RIIO-GD3) which will take us into the 2030s.

Trusted partner

Net zero is the defining challenge of our age. We aim to be a trusted partner to Government, industry and our customers through the energy transition.

We believe in a 'whole systems' approach, including the development of the UK's hydrogen economy. That is why we are delivering to help make that a reality.

We are committed to building a thriving and enduring SGN.

Our H100 Fife project, due to go live in 2024, will be the first 100% green hydrogen-to-homes zero carbon network anywhere in the world, providing important evidence to help the UK decarbonise home heating.

We are also assessing the viability of repurposing the local transmission system from natural gas to 100% hydrogen. These are just two significant projects which could change the way we use energy today.

The work we are doing now will help keep our customers safe and warm while making SGN a more sustainable, inclusive business for many years to come.

Mark Wild OBE
Chief Executive Officer
27 July 2023

SGN at a glance

The SGN Group owns one of the UK's largest and most innovative gas distribution networks, operating across Scotland, southern England and Northern Ireland.

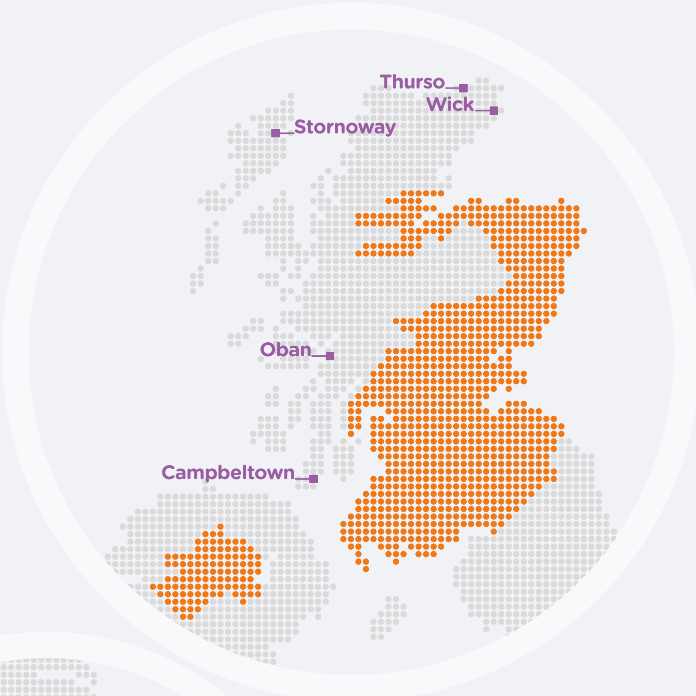
24 hours a day, seven days a week, 365 days a year, our teams are working behind the scenes and out on the streets looking after our 74,000km of pipe network – keeping you safe and the gas flowing to six million homes and businesses in the south of England and across Scotland.

Our purpose

Serving our communities by keeping everyone safe and warm.

Our vision

To give our customers the best clean energy experience.



Operations throughout the UK

Scotland

Our Scotland network distributes gas across all of Scotland to 75% of households, including remote areas through the Scottish Independent Undertakings (SIUs) at Stornoway, Wick, Thurso, Oban and Campbeltown.

Northern Ireland

In Northern Ireland we are now fully operational with our High Pressure (HP) and Intermediate Pressure (IP) pipelines built and connected. We have also connected a number of large industrial and commercial (I&C) customers and continue to build our domestic customer base.

Southern England

Our Southern 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, distributing gas to around 90% of households.

Key

- SGN head office
- SIUs

The SGN brand portfolio

As our business expands so does our portfolio of brand identifiers under both our regulated and non-regulated activities.

Regulated business

Our regulated businesses form the core of our activities in providing a safe and secure supply of gas to our customers throughout our three gas networks.

SGN Your gas. Our network.
SGN Natural Gas

Non-regulated businesses

Our non-regulated activities are closely aligned with our core business activities, ensuring management understanding and decision making comes from a position of knowledge and experience.

SGN Commercial Services
SGN Connections
SGN Heat Networks
SGN H100 Fife
SGN Metering
SGN Place
SGN Futures

Operating review

Our purpose, vision, and values

Our values have always demonstrated what we stand for as a company and help guide us to achieving our vision and goals. They not only dictate the way we behave but also help us build trust, so we can thrive as both individuals and as a company.

This year we took the opportunity to refresh our purpose, vision, and values. We did not introduce wholesale change, instead building on what we had already and developing them from where they were, reflecting our own progress as a company and the evolving societal values that surround us.

In order to maintain their authenticity and relevance we asked, and listened to, over 1,000 of our people. This ensured we were able to reflect in these values, what matters most to them.

It is important that values are not just another set of words or a poster on the wall, but that people live up to them every day.

Watch **OUR STORY** here

Safety

While our track record on safety is good, we strongly believe that it can be great. We want SGN to be a zero-harm business and make sure we can get everyone home safe and well.

We recognise that the health and safety culture of an organisation is a major influence on shaping people's safety related behaviours and consequently improving the culture of SGN is our number one objective.

To achieve our goal of zero harm, we will ensure we learn from recent incidents and develop and coach our people, so they are able to demonstrate excellent leadership with all employees realising the impact that their actions have on others. We want everyone to inspire others to work and behave safely, no matter what their role is.

We will strive to become a business that listens to our people and will provide mechanisms for engagement with front line workers, to achieve a position whereby all employees feel valued, trusted, and empowered.

At the same time, we will expect our people and contractors to take ownership and responsibility for their safety and that of others, always taking time to ensure the highest standards of safety are achieved.

It is important that values are not just another set of words or a poster on the wall, but that people live up to them every day.

Our high pressure pipework in the south of England.

Cyber security

We continue to be active and vigilant in our work to identify and mitigate potential cyber attacks on our IT and OT systems and infrastructure. As part of the UK's critical national infrastructure, we are a target for cyber criminals from around the world motivated by financial gain or political activism, and possibly funded by hostile nation states.

To minimise this risk, we have a long-term and substantive cyber security investment programme, on the progress of which we regularly update Ofgem and senior stakeholders.

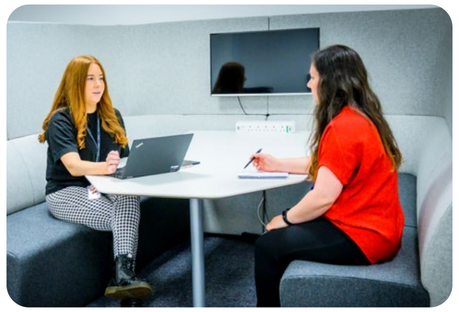
As one of our highest corporate risks, cyber security is an Executive and Board matter. We know and understand that this is a constantly evolving threat that requires rigorous attention and action.

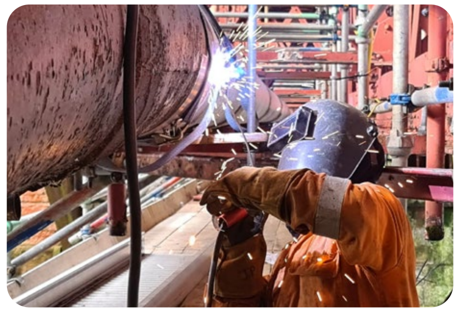
Operations

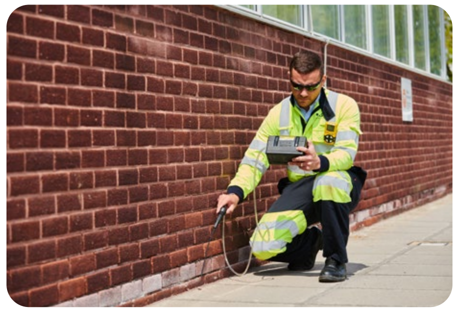
During 2022/23, we attended over 184,800 gas escapes across our Scotland and Southern network areas.

We invested £256.7m in delivering our replacement policy mains, non-policy mains, risers and other replacement projects.

Across our Scotland and Southern networks, we replaced 789.4km of gas mains with polyethylene pipe, ensuring we can continue to deliver gas safely and reliably for many years to come.







Providing a friendly face with care and advice for customers.

Using innovative techniques such as CISBOT and Core and Vac, we were able to complete replacement jobs with minimum disruption to our customers as we only need to excavate a small section of the public highway to complete our work.

We delivered against our maintenance targets for 2022/23 in both our Scotland and Southern networks.

In Scotland, we achieved 99.3% of our scheduled maintenance activities and it was a similar story in Southern where we delivered 97.7% of scheduled maintenance activities across our asset bases.

Major projects

We performed well with large-scale replacement projects, consistently completing complex programmes under challenging circumstances in record time.

Routine maintenance

As part of our routine maintenance of the high-pressure transmission system we carry out regular inspections on all our above ground crossings. These are locations where our high-pressure pipelines come above ground to cross either railways, rivers or roads with some sites more accessible than others.

One inspection we carried out in 2022/23 was on a pipeline attached to a Network Rail viaduct at Uddingston which crosses the River Clyde.

The pipeline crossing the Uddingston Viaduct is contained within a protective sleeve for the 90m of bridge. The sleeve is designed to protect the pipeline from impact and also to prevent corrosion. We do this by filling the sleeve with nitrogen, which creates an inert environment, preventing any corrosion from developing.

Once we had safe access, we were able to inspect each support, repair the interface between the supports and the sleeve and then recoat the whole pipeline, protecting it for another 40 years.

Resilience

Every year we participate in a range of different external resilience meetings and exercises, many involving various emergency services, voluntary organisations, and local authorities. Our relationships with the local authorities covering our southern England and Scotland regions are extremely valuable, as together we aim to always protect and look after our most vulnerable customers.

Kennington Oval
Manoeuvring the tee piece into position, ready for installation.

Focused on the network

One of our major projects is taking place at Kennington Oval where we are diverting the gas main and relocating the triple stream governor.

For the first time ever on our network, we used 800mm of polyethylene pipe instead of two lengths of 630mm LP gas mains.

To support with the operation, we turned to fellow Gas Distribution Network Cadent, for some expert advice on butt-fusing the 12m lengths of pipe together. Almost 50m of 800mm polyethylene pipeline was laid along Kennington Oval, ready for connecting to an existing 36" cast iron LP main.

During the project, we negotiated a one-way system with Lambeth Council where we had to hold back traffic. Our contractor Phoenix Civils handled this perfectly, using team members to walk the route keeping everyone informed.

The section of the highway where we needed to install a connection was heavily congested with other utilities. To overcome the problem, we installed a 30" equal tee, a bespoke fabrication carried out by Flowstop Services.

We fabricated a tee with a subtle bend in the outlet to help it manoeuvre through the multiple utilities in the excavation. After careful manoeuvring, we bolted the 1.5 Tonne 30" equal tee into position and installed a valve, ready for connection to the 800mm polyethylene gas main we had already installed.

We have since installed a 'spherical tee' on our IP main, a first for the UK gas industry. This technique was utilised as a different solution to the conventional welded split tee and horizontal drilling due to lack of space for the drilling rig.

Our project at Kennington continues and we hope to have it completed by August 2023.

Damage prevention

We continue to work with partners across our operating regions to raise awareness and actively prevent third parties from damaging our gas network. This is important, not only to stop anyone being injured, but also to ensure our customers are not inconvenienced or worse, from losing their gas supplies.

Gas Control Centre

Operating 24/7, our Gas Control Centre forecasts our customers' gas demand, stores the gas required to meet this everyday demand and monitors and responds to any alerts received in our high-pressure sites.

To help the transition to net zero, our Gas Control Centre is also monitoring many biomethane sites which are connected to our gas networks or through a facility to bring gas that is not directly connected to the national network, such as into our Portsdown Hill injection facility near Portsmouth in Hampshire.

We also continue to support the import of gas from Liquefied Natural Gas (LNG) which arrives on ships into the Isle of Grain.

Recruitment

2022/23 saw 40 new apprentices arriving into our business and saw our biggest ever recruitment drive begin. With 600 operational roles to fill, we are doing everything we can to promote SGN as a company who cares. It is a cross-team effort with colleagues from right across the business getting involved in our recruitment drive. This will help us to re-resource our business and help us continue to serve our communities by keeping everyone safe and warm.

We are also committed to bringing in 120 new apprentices and trainees into the business each year, for the next three years, helping to develop them into our engineers of the future. Something which is extremely important as we will need new skills to help us with the decarbonisation of the UK's gas network.

SGN business model

While our business model has been developing since our inception in 2005, we have been careful to ensure our endeavours relate to our core activities while increasingly looking to maximise the potential of our engineering assets and the experience and skills of our people.

Inputs

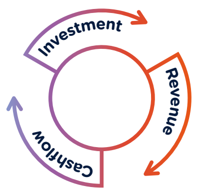
Financial
We make use of our external borrowings and shareholder capital to run our business and deliver a safe and efficient network for our customers.

Social
We provide a public service supplying gas to those who need it, keeping our 5.9 million customers safe and warm while our people play a key role in wider society looking after the communities we serve.

Physical
We keep our operational assets well maintained and in fully operational order to ensure the safety of the public. In support of our business, our IT assets and infrastructure have been upgraded and are protected from external cyber attack.

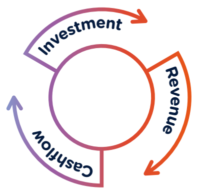
Core activities

SGN



Essential to running a safe and efficient network is understanding the regulatory requirements and delivering on the outputs set.

SGN Natural Gas



Completion of the Gas to the West project in Northern Ireland provided us with a third national network and a natural extension to our gas network portfolio.

Non-regulated businesses

SGN Commercial Services
SGN Place
SGN Metering
SGN Futures
SGN Connections
SGN Heat Networks
SGN H100 Fife

Our non-regulated activities are closely aligned with our core business activities.

Outputs

SGN:
- To facilitate the delivery of service excellence to our customers, invest and safeguard the network and provide safety and security to all users.
- Aiming for a range of collaborative projects with other GDNs to secure a future for the gas networks as part of a decarbonised energy system.
- Looking to provide extra help to the most vulnerable in our society.

SGN Natural Gas:
- Third gas network built and operating in Northern Ireland.
- Potential for 40,000 new gas customers to receive natural gas.
- Providing a cost effective fuel and help tackle the issue of fuel poverty.

Non-regulated businesses:
- Providing expertise in the development of biomethane plants and associated green gas production.
- Providing a focus on the adoption of gas and electricity infrastructure assets across the UK (including vehicle charging points).
- Providing new gas connections to benefit society and the wider UK economy.
- Targeting a leading market position on developing, owning and operating heat networks throughout our regions.

The journey to net zero
We are taking a strategic approach to decarbonisation to develop pioneering clean energy projects to help shape the UK's future.

Our vision is to give our customers the best clean energy experience. We strongly believe that decarbonising the gas networks, predominantly through the adoption of hydrogen in place of natural gas, can play a vital role in helping meet the UK net-zero targets.

While we do not see hydrogen as a silver bullet to decarbonise home heating, we do think the scale and complexity of the challenge is so big that we are going to need every tool in the box to achieve it – that means hydrogen, biomethane, heat networks and electrification.

We must develop a whole system understanding of the impact of these technologies, while being clear on the potential cost of different pathways to consumers.

As the UK and Scottish governments have acknowledged, hydrogen will have a role in decarbonising the power and industrial sectors while ensuring we maintain security of supply and capture the economic benefits that net zero offers.

The power stations that take supply from the gas network will play an essential role in maintaining security of supply, balancing nuclear and renewables. And with industrial load located not just in key clusters but across our entire network, we must find a way to distribute hydrogen efficiently to enable this. Which is why projects such as Local Transmission System (LTS) Futures are essential.

On the coldest day of this winter, SGN supplied the gas equivalent of 11GW of power to our customers in Scotland. In whatever form it comes, a huge transformation needs to take place to decarbonise that gas and at SGN we are sure hydrogen will be part of that.

It is essential that the whole system cost to consumers of different pathways for decarbonising residential heating is understood by policymakers, regulators, and the industry. We need solutions which work with customers and the challenges they face in managing their household budgets.

We must also look at the next great challenge of net zero on a whole system basis and understand how we design and build infrastructure that optimises the resources we have across multiple sectors.

We will be giving this a lot of thought in the next year and expect it to be central to our approach in the future.

Improving our fleet
We had plans to transition around half of our new commercial fleet to become a zero emissions fleet by the end of the current regulatory price control (2026). Unfortunately, current vehicle supply issues and a shortage of operationally suitable vans have delayed the plan. We have taken delivery of our first batch of 25 electric vehicles which are being put through their paces in our Southern and Scotland regions.

Over the last 12 months, we have introduced 42 electric cars and 66 hybrid cars as part of our Company car fleet. To further encourage electric car usage, SGN reimburses colleagues at a higher rate of business mileage than that recommended by HMRC.

Our fleet team is working hard with suppliers to secure our new vehicles as quickly as possible. However, along with many companies around the world, we are facing challenges and delays to delivery dates.

While we are waiting on a backlog on vehicles being delivered from this fiscal year (2022/23), we are expecting over 550 vehicles to be delivered in 2023/24, which will help to enhance our ageing fleet.

Commercial Services and ventures
Commercial Services and ventures cover our non-regulated activities. We maintain strict business separation principles between the regulated and the unregulated business activities.

Biomethane
SGN Commercial Services is continuing to develop its biomethane, gas to grid business and building on its leading market position, helping to green the gas network and provide a route to market for biogas producers.

SGN Commercial Services won a framework contract with Thames Water in 2021 to deliver gas to grid injection plants across Thames Water's wastewater treatment works.

The initial project at the Deephams sewage treatment facility was commissioned in April 2022 and work has begun on a second project at Mogden, near Twickenham, and is targeted for completion in September 2023.

Each site will turn sewage into biomethane for a heat and power alternative to help offset thousands of tonnes of carbon dioxide from entering the atmosphere each year.

Given the success of the framework, the business model has been further developed and refined and work is under way to enter similar agreements with other water companies in the 2023/2024 business year.

Heat networks
The SGN Vital Energi joint venture is supporting the SGN Place Wandsworth property development with a hybrid energy solution.

The development, located on a former gas holder site in the centre of Wandsworth town, will be a mixed-tenure scheme including both commercial property and 637 homes, comprising four main buildings ranging from 10 to 30 floors.

A combination of new planning regulations, grid capacity constraints and London's target to reduce carbon emissions has led to the design of a new technical solution

Repurposing the network for hydrogen

Left to right: Chris Park, H100 Fife Project Director; David Ross, Leader of Fife Council; Mark Wild, Chief Executive of SGN; and Ken Gourlay, Executive Director of Fife Council dig the first sod at the start of the building phase of the H100 Fife Project.

Focused on the UK's energy future

Offering a similar customer proposition to natural gas, we are exploring whether the pipes we manage could be repurposed to take on hydrogen in the future.

At the domestic level, our world-first H100 Fife project will soon deliver green hydrogen to homes in Levenmouth, Fife and 2023/24 will see us reach several key milestones.

In March 2023, we celebrated a major milestone for our world-first H100 Fife project when we officially started construction of our hydrogen demonstration facility.

The demonstration facility will have two hydrogen show homes where visitors can try out domestic hydrogen appliances and is due to open during the next fiscal year in Fife Energy Park near the homes that can sign up to H100 Fife.

These exciting developments build on news in mid-February that we have also appointed leading engineering firm Altrad Babcock as the main works contractor for the hydrogen production and storage site.

H100 Fife is due to go live in 2024 with 300 households who have volunteered to take part in the project. It will be the first 100% green hydrogen-to-homes zero carbon network anywhere in the world and will provide important evidence to help the UK decarbonise home heating.

In the UK, we have an opportunity to scale up the production of indigenous hydrogen, working alongside electricity, to help deliver a resilient system that decarbonises several sectors and opportunities to go further are plentiful.

for the development's district heat network and plans to utilise waste heat sources in the area.

The Government's Heat Network Zoning programme estimates the heat network market will require a £60bn to £80bn investment and the Department for Energy Security is planning pilots expected to start as early 2025.

Commercial Services and metering

We have secured further opportunities on our maintenance and emergency response contracts where we maintain over 500km of high-pressure pipelines for third parties across the UK and Northern Ireland. We have also re-secured a ten-year contract to control and monitor Mutual Energy's Northern Ireland gas network through our centralised Gas Control Centre.

In addition, we have been working to provide biomethane connection services to three North Ireland gas networks who are expecting a significant increase in biomethane plants in Northern Ireland to support the Government's decarbonisation efforts.

We have also completed some pilot projects to test the viability of reusing our decommissioned gas pipes as ducts for non-gas utility infrastructure, such as new fibre optic, telecoms, or water networks. We are also promoting the shared use of some of our redundant landbank for the same purposes.

Murphy Utility Assets (MUA)

Our 50:50 joint venture with J Murphy and Sons, focused on last mile utility infrastructure adoption, has been successful in securing a significant share of the new build market. In the year 2022/23, MUA was able to raise a £30m debt facility with Santander to fund the continued growth of the business and has plans to target new markets and increase its services beyond gas and power infrastructure.

FYLD

FYLD is a mobile field force safety and productivity app that was developed by SGN to support its frontline operatives and SGN holds

Operating review

a minority share in the FYLD business. The FYLD business continues to grow its market presence and has expanded into new international markets including North America and has also developed a presence in adjacent infrastructure sectors winning contracts with water and transport clients.

An authentic leader in customer care

Keeping our six million customers safe and warm is at the heart of everything we do.

We are particularly pleased to report, that for the seventh year running, our Scotland network remains the UK's number one gas distribution company for customer satisfaction.

This is great testament to the hard work and dedication of all our people who are focused on providing a 10/10 service every time and always putting our customers first.

Our Scotland network recorded an impressive score of 9.30 out of 10. Although our Southern network is in eighth position, it still achieved a score of more than 9 (9.02) as we promised in our RIIO-GD2 business plan.

Keeping the most vulnerable customers across our regions safe and warm is an undoubted priority.

To deliver on our commitment to make a positive impact on society by supporting vulnerable customers and to guide our activity, we have worked with consumer vulnerability and gas safety experts to develop a dedicated vulnerability and carbon monoxide strategy.

This year alone, we have supported 118,731 households with the initiatives we have in place.

Fuel Poor Network Extension Scheme

This year we have connected a total of 649 customers as part of the FPNES – 199 customers in Southern and 450 customers in Scotland.

This is lower than 2021/22 as we had no large projects carried over from the previous year and the impact of the removal of gas boiler and appliance funding under Eco4, meant fuel poor households do not have access to the financial support they need to install a gas central heating system and boiler.

The impact of net zero and UK Government Policy has impacted the ability of all Gas Distribution Networks (GDNs) to help support fuel poor households connect to the gas network. However, Ofgem agreed with all GDNs they could repurpose some of the underspent funding this winter to support those in need gain access to much need services using our VCMA criteria.

This has allowed SGN to partner with national and community partners in both networks allocating £900k of the funding for additional support to help keep fuel poor households safe and warm.

Biomethane plant in Coupar Angus, Scotland.

Our community partnerships

watch how the VCMA is supporting customers

So far, we have co-designed more than 30 unique initiatives with partners through the VCMA developed by Ofgem.

It is through building these partnerships with trusted community support agencies that we have been able to quickly help existing support services by increasing available funding and capacity during the cost-of-living crisis.

More than ever, people are seeking out support in the most unlikely of places to keep warm and access support to help keep homes warm.

Here are some of our partnerships that we are most proud of.

Safe & Warm community scheme

Over eight million UK households live in fuel poverty. This means a significant number of people live in homes they cannot afford to heat.

Access to crisis support, as well as accurate and accessible advice and information to help people remain warm in their homes is vital, particularly for people in vulnerable circumstances or struggling on a low income.

More than ever, people are seeking out support in the most unlikely of places to keep warm and access support to help keep homes warm. That is why we have joined forces with the Centre for Sustainable Energy (CSE) to provide a £500,000 grant for local charities and support groups to help people who are most affected by the cost-of-living crisis.

The scheme will share a funding pot of £500k to create a network of 12 to 20 grassroot community organisations who can provide much needed support for communities in energy crisis.

Through the scheme, we are aiming to reach over 5,000 customers who need help to keep their home safe and warm.

Raising CO awareness

We are leading on a partnership with the other Gas Distribution Networks (GDNs) to support over 17,500 vulnerable people using the Citizen Advice Energy Advice Programme.

The partnership saw Citizens Advice raise awareness of carbon monoxide (CO) and reduce CO risk for vulnerable people.

Levenmouth Academy pupils visit our demo kitchen in Fife Renewables Innovation Centre.

Our pipeline at one of our offtake sites.

We trained its teams on CO awareness (designed for frontline workers), to enable them to add this and the co-designed energy advice and safeguarding packs, which include a free CO monitor to households unable to afford to buy one themselves.

Through our partnership, Citizens Advice was able to extend its Energy Advice Programme to an additional 5,000 vulnerable people. This helps Citizens Advice give in-depth energy advice and support sessions for people who need it most.

Alongside the other GDNs, we have led on a partnership with The Scout Association to help teach young people about the dangers of CO, and how to keep them and their families safe from the 'silent killer.'

We have worked together to launch activities for all age groups between 6 to 18-year-olds, helping them to understand the signs of CO, the symptoms of CO poisoning and what steps to take if they think the poisonous gas is present in their homes.

We have also sponsored the Cubs Home Safety Activity Badge. Cubs will now be able to earn their badge when learning about CO safety, how to prevent accidents in the home, and gain knowledge on what to do if they happen.

Operating review

Safe & Warm team hub
Our Safe & Warm community officer giving advice about carbon monoxide to a member of the public.

Focused on customer care

In our most recent customer focus groups, we learned that our customers would value extra help and advice with energy support services offered on site as we go about our works.

Partnering with Haste, we have brought a team on to work alongside our operational and contractor teams to provide energy and community support services.

When on site, our Safe & Warm team check in with our operations teams, set up our mobile hub and door knock customers identified as potentially vulnerable.

We have been piloting the service for the past six months and initial feedback from customers is that it has gone down extremely well, and they have felt better looked after by our teams as a result. We plan to further embed this service across our whole network area to make sure we never have to walk away from a customer in need.

UK Customer Experience Awards

Gold awards for:
Best Customer Centric Culture
Vulnerable Health and Wellbeing

Bronze awards for:
Best Customer Service
Customer at the Heart

Safe and warm additional services

As provider of the national gas emergency service in both Scotland and southern England, there are times when we must isolate a customer's gas supply to keep them safe in an emergency. If the cause of the gas emergency is an issue with internal pipework or a faulty appliance, we must advise them to contact a Gas Safe registered engineer to complete the repair.

We recognise that vulnerable customers might not have the finances or resources to make the repair and restore their gas supply. Our additional services are there to provide an emergency funding referral service for our engineers to pass on to any vulnerable customer where they have had to isolate the gas supply or condemn an essential gas appliance.

This service is offered to eligible vulnerable customers who are unable to afford the costs associated with servicing, repairing and/or replacing gas pipework or gas appliances. We also offer additional support services best suited to their circumstance, such as:

- Gas safety advice and raising awareness of CO
- Energy efficiency advice and onward referrals for energy efficiency measures
- A working CO alarm if there is not one at the property
- Access to additional support services for our vulnerable customers, suited to their needs
- Registering vulnerable customers on the Priority Service Register (PSR) for energy and water

Together with our partners, we have been able to help over 118,000 households, those most at risk of living in a cold and unhealthy home, with support that helps them stay safe and warm and, in some cases, independent in their homes for longer.

Innovating to improve safety and efficiency

Our commitment to continuous innovation and improvement is showcased below and details many new and exciting products and processes, with our key focus always being on improving safety and efficiency.

Smart digging

click here to see **AUSMOS** in action

Automated Utility Service Mark-out System (AUSMOS)

Overview

AUSMOS accurately scans the road surface to create a digital map of utility assets underground.

Across the UK, utility companies perform over four million excavations annually to undertake various work on their assets. Failure to accurately identify the location of existing buried assets impacts safety, the environment and causes public disruption, especially in urban areas like London.

When excavating the road, many utility companies (including SGN) rely on drawings – either on paper or digital format – however, current mark-out practices have limitations and, on occasion, can present a threat to assets from cable strikes due to the limitations in sensor accuracy.

These asset strikes impact on the health and safety of our workers, the public and create disruption during unplanned repairs.

Creating a digital map that holds this information would make it safer to dig, helping workers to avoid hitting dangerous and costly pipes and cables.

It will also increase efficiency, allowing works to be completed more quickly and reducing disruption on the road network.

AUSMOS aims to transform a traditionally analogue process in marking out underground assets.

AUSMOS will use robotics, Artificial Intelligence (AI) and Machine Learning (ML) to precisely identify all underground utility assets. With higher precision and accuracy, AUSMOS can benefit all roadworks activities to improve safety and efficiency.

Using electromagnetic sensors and Ground Penetrating Radar (GPR), a prototype of AUSMOS has been field trialled on our network where it was successful in identifying the underground assets by generating a 3D model. This permitted the accurate markup of the road surface and knowing what asset was buried where and at what depth, which reduced the overall cost and length of the project.

Status
In development.

Less landfill

Core and Vac MK2

Overview

Core and Vac eliminates the need for large excavations by removing a small section of road (the core) allowing our teams to access the gas pipe.

When carrying out excavation activities, we conventionally require large excavation works to allow our engineers to work safely below ground within the trench. These excavations on the carriageway cause disruption to traffic flows for extended time periods and have an impact on the environment, with the disposal of excavated material and the import of either virgin or recycled backfill material.

This project develops an improved Core and Vac vehicle to reduce occupancy time on highways by faster coring, more efficient air pick/vacuum technology and reinstatement completed within a single day.

Using the latest innovation in core and vacuum technology, the system improves efficiency, further reduces time on site and reduces the amount of excavated material sent to landfill – helping to minimise our impact on the environment.

Over 60 repair jobs have now been completed using the new Core and Vac system.

Case study

On the extremely busy A3 northbound road into Wandsworth, we had to repair a leaking joint found in the carriageway. The road was further complicated as it came to a pinch point where it goes from three lanes into one.

To gain access to the asset, we needed to install a two-way traffic light system and close a side road and bus stop. Conventionally, this operation would have taken four days to complete.

With the new Core and Vac system, we completed work within six hours which also included setting up the traffic management. To minimise disruption for road users, work started after morning peak hours at 11am and all repair and reinstatement was complete before evening peak hours at 5pm.

Long handed tooling also allowed our engineers to complete the repair above ground through a small keyhole of 600mm.

Status
In field trials.

Innovating to improve safety and efficiency

World first

Stent bag

Overview

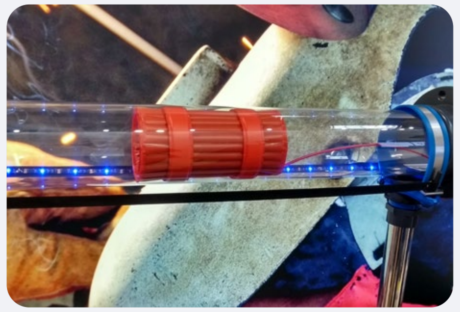
The stent bag works like a heart stent by sealing any leaks in pipes that carry gas. We inflate the bag inside the pipe to stop gas from escaping, while still allowing gas to flow to the customers who need it.

The stent bag allows a gas escape to be remotely stopped from inside the gas main while maintaining the flow of gas to our customers.

It is a world-first to carry out this type of work on gas pipes – the concept is similar to stents used in the medical industry where a wire mesh tube, with a balloon catheter is inflated, reopening the blockage, and the stent expands and locks into place.

This equipment allows for a much safer and quicker approach to managing high volume gas escape scenarios, leading to improved safety for our employees and members of the public.

There are also significant environmental benefits in deploying the stent bag during a repair, as any release of gas into the atmosphere can be vastly reduced or even stopped, while maintaining the gas flow to our customers.



Case study

We have been putting this equipment to good use and so far, it is making a huge difference. On one job and without the stent bag, if we used conventional means we would have required approximately seven engineers to carry out the work and needed to open six excavations just to get the work done.

Using the stent bag meant we needed fewer engineers, reduced the number of excavations to carry out the repair and also reduced the need for traffic management, meaning less people were impacted as a result of our work.

Not only does the stent bag keep our people safer, as they are excavating further away from the gas leak, but it also offers considerable time and carbon savings too.

Status
Rollout started.

Breaking barriers

TapSOS

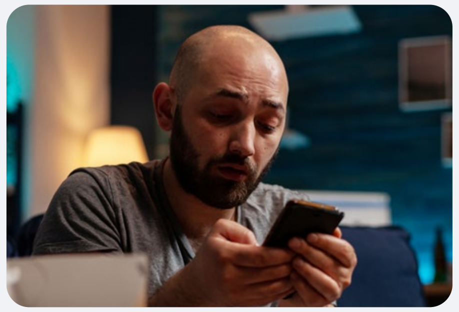
Overview

By digitally transforming an emergency reporting solution, GDNs enable even greater inclusivity and give all consumers greater confidence in communicating with the distribution network.

Communication with gas networks can be challenging, particularly for consumers in vulnerable situations as they may struggle to communicate or understand what is being said due to physical, medical or situational barriers.

Across the UK, 12 million people are registered deaf or hard of hearing, 87,000 rely on British Sign Language, 700,000 people are on the autism spectrum and 1.25 million people living in the UK are non-English speaking.

These challenges sometimes lead to unnecessary calls and difficult triage, slow responses, over-deploying of resources in the field and inaccurate information handling. All of which can cause frustration, anxiety and stress for the consumer and overspend for the provider.



Partnering with TapSOS/Inclutech and the other Gas Distribution Networks, we are working together to design and develop a digital solution with which our customers can use to contact us.

This solution will enable us to meet Ofgem's regulatory requirements and recommendations, outlined in its vulnerable consumer report.

Status
Phase 1 – Feasibility study and wireframes completed.
Phase 2 – Due to start soon.

click here to see TAP SOS in action

Market leading

Predictive safety

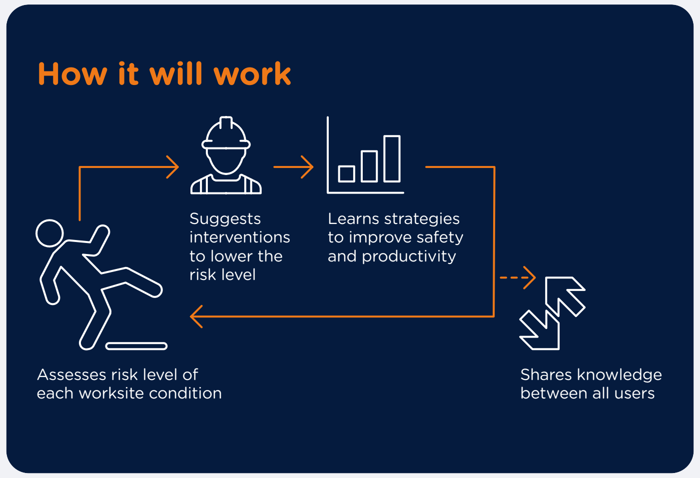
Overview

An artificial intelligence model to enable Predictive Safety Interventions.

Through the Discovery and Alpha phases, FYLD and SGN partnered to produce an artificial intelligence model to enable Predictive Safety Interventions. The predictive model is trained on safety indicator event data, and previous near-miss and injury occurrences, to accurately forecast the likelihood of an injury occurring to a fieldworker.

The Beta project phase will develop this model further, increasing data inputs into the model to include human behaviour factors.

We will integrate fatigue levels into the predictions, and test and research the ability to detect changes in voice tone or pitch as an indicator of how human behaviours impact safety events.



We will also integrate live network data, such as traffic and roadworks, alongside further development of the object-recognition model.

The project will build the capability to deliver an AI powered personalised intervention pushed directly into the hands of field teams and their remote managers.

This will enable the near automation of sharing of learning from previous safety indicator events, including near misses and injuries, directly to the front-line on high-risk activities. The project will then progress to deploying the prediction model to all of SGN field operations to successfully reduce safety incidents.

Status
Discovery and Alpha stages complete. Application for Beta submitted to Strategic Innovation Fund (SIF) (March 2023).

Overview
Strategic Report
Governance
Financial Statements

Engaging with SGN stakeholders

We believe we make better decisions for our customers and stakeholders when we understand their needs and priorities.

SGN key stakeholder groups

We encourage genuine two-way engagement with our six key stakeholder groups to gain valuable insight and expertise to help inform our decision-making.

Updating key stakeholders on our H100 Fife project.

Engaging with our stakeholders is fundamental not just to our day-to-day activity, but also to the long-term success of our business. It's this invaluable, continual insight generously shared by our wide range of stakeholders that helps the Board shape policies and practices, best predict future developments, and react to emerging threats and trends.

"Our job is to serve our customers, the communities in which we operate and our staff. Their input, insights, knowledge and guidance is crucial to our success in delivering the best outcomes for them. We listen, learn and act on their input."

Laura Sandys
Stakeholder and ESG Committee Chair

2022/23 activity

Stakeholder engagement takes place at both the operational day-to-day level within the business and at Board level, as part of an extensive engagement programme with our six key stakeholders:

- Customers
- Our people
- Government and regulators
- Communities and the environment
- Suppliers, contractors and partners
- Shareholders and debt investors

The Board takes insight from each level of engagement into account in its decision-making process.

Following the lifting of Covid-19 restrictions, we conducted a mixture of face-to-face and virtual engagement to ensure that this remained inclusive and allowed for a two-way dialogue with our stakeholders.

The panels that follow set out some of the most notable ways in which we engaged with each of our six key stakeholder groups and, where relevant, the impact of that engagement on our strategy.

Customers

We keep gas flowing safely and reliably to six million homes and businesses, all day, every day.

Why we engage

Understanding our existing and future customer needs and behaviours help us to achieve our vision of giving our customers the best clean energy experience.

How we engage

- Customer forums, focus groups and research panels.
- Customer satisfaction surveys.
- Our Customer and Stakeholder Engagement Group (CSEG).
- Our Vulnerability Steering Group.
- Our website and social media channels.

Stakeholder issues raised

- Changes in customers' expectations relating to service delivery and customer experience in the post-pandemic era.
- Regulatory changes pertaining to customer satisfaction performance, guaranteed standards of service and support for customers in vulnerable circumstances.
- Customer experience is impacted by behaviours of our people, quality of communication, information quality, and efficiency of processes and timescales for delivery.

Outcomes of engagement on key decisions

- We have further invested in customer experience and data interrogation to understand the drivers of customer contacts and complaints, which has led to a steady reduction in inbound contacts.
- Utilisation of digital channels including live chat and two-way SMS has enabled more efficient resolution, and improvements in service have included PayPal integration, speech analytics and application portal improvements.
- The Board continues to regularly meet and obtain feedback from the Customer Engagement Group.

Key Board decisions

- Investment and implementation of the customer strategy to continually improve and strive for number one in customer satisfaction across GDNs by further enhancing our responsiveness, implementing proactive measures and improved data and insight to predict where issues may occur in the future.
- Approval of the annual health and safety targets for the financial year which impacts customers and other stakeholders.

Our people

We employ approximately 4,000 highly skilled and dedicated people across Scotland, the south of England and in Northern Ireland.

Why we engage

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

How we engage

- SGNapp, Energy FM, Yammer and DigitalHub.
- Town hall sessions, Team Talk, employee networks, CEO coffee sessions and safety briefings.
- Trade union and pension trustee engagement.
- Diversity and inclusion networks.
- Annual employee engagement survey.
- In person confidential engagement sessions between the Board and our people.

Stakeholder issues raised

- Cost-of-living crisis and pay.
- Availability of resources, vans and equipment.
- Post-pandemic desire for more flexible ways of working.

Outcomes of engagement on key decisions

- Conducting a benchmarking exercise on pay.
- Additional investment in resourcing and procurement of essential tools and equipment, including operational vehicles.
- Supporting the implementation of the flexible working model developed following the workplace review.
- Working with relevant unions and stakeholders to ensure SGN operates as fair employer.
- Continued reporting on performance of the stakeholder issues raised at every meeting of the Board and bi-monthly CEO Board update calls.
- Continued focus and discussions on safety of our people, Company culture, diversity and inclusion, employee training programmes, retention and recruitment, fleet given the issues raised.

Key Board decisions

- Communication and cascading of key insights and actions to SGN leadership team.
- Approval of strategic architecture to deliver excellence today and assist in the transformation of SGN for a decarbonised future.
- Support to invest further in the resourcing of direct labour.
- Approval of the recommendations presented following the benchmarking exercise regarding pay for our people.
- Approval of SGN's Code of Conduct which additionally includes expectations regarding culture, safety, diversity and inclusion for our people.

Engaging with SGN stakeholders

Government and regulators

We work constructively and collaboratively with both UK and Scottish governments as well as regulatory bodies such as Ofgem, UREGNI and the HSE.

Why we engage

Understanding what drives government and regulatory policy decisions helps us to ensure we deliver on our regulatory outputs to keep our customers safe and warm.

How we engage

- Senior government and regulatory engagement is led by the CEO on behalf of the Board. The type of engagement includes:
  - Bilateral meetings;
  - Attendance at round tables;
  - Government/industry working groups.
- The CEO also has oversight of formal government and regulatory consultations that has material impact on our operations and customers.

Stakeholder issues raised

- Price controls.
- Supplier of last resort.
- Decarbonisation of gas.
- Cost-of-living crisis impact on fuel poor and vulnerable customers.
- Cyber security.
- Operational resilience and security of supply.

Outcomes of engagement on key decisions

- Continued investment in our Cyber Security Programme to put in place additional precautionary measures to mitigate increasing threat levels.
- Cyber Security Resilience briefing by Ofgem received by the Board.
- Provision of wider support for the Company for increased political engagement on decarbonisation.
- Support with the development of a solution to Supplier of Last Resort (SoLR) claims arising from the financial pressures on gas suppliers.

Key Board decisions

- Approved the submission of the Company's response to Utility Regulator of Northern Ireland's Draft Determination for the GD23 Price Control.
- Approval of continuing investment in our Cyber Security Programme to help meet government and regulatory requirements and National Cyber Security Centre standards.
- Approval to increase political engagement on key issues such as decarbonisation and consumer vulnerability.
- Agreement to re-purpose SGN's unused fuel poor network extension scheme allowance to support vulnerable customers.

Communities and the environment

We've established multiple strategic and long-term partnerships with third-sector organisations representing hard-to-reach and vulnerable groups within our communities, as well as environmental bodies.

Why we engage

Engaging with communities enables us to build our shared net-zero future by accelerating decarbonised energy solutions and minimising our environmental impact, while also ensuring the support we provide to vulnerable groups is delivering tangible benefits to those most in need of help to stay safe and warm at home.

How we engage

- Community liaison groups.
- Drop-in community events and virtual workshops.
- School assemblies and hydrogen education workshops.
- Our Environmental Advisory Group.
- Our Vulnerability Steering Group.

Stakeholder issues raised

- Carbon impact associated with operating our business.
- The role of green gases in the transition to net zero carbon emissions.
- ESG performance and Task Force on Climate-related Financial Disclosures (TCFD) reporting.

Outcomes of engagement on key decisions

- We have entered into a commercial partnership with Yorkshire Water for two gas-to-grid biomethane projects in Leeds and Sheffield, utilising anaerobic digestion of waste sourced from wastewater treatment plants.
- Biomethane is currently producing c.19TWh of biogas in the UK, which is enough to heat 1.6 million homes and has the potential to provide enough gas to offset natural gas demand of 6.4 million homes, reducing emissions by 6%.
- Focused discussion on shrinkage performance, and innovative activities to drive down emissions.
- Continued performance reporting on SGN's operations and Repex delivery programme at Board meetings.
- Conducted a dedicated Energy Futures strategy session covering hydrogen and the journey to net zero.
- Development of the Environmental Action Plan and communities' investment strategy.

Key Board decisions

- Approval of the gas to grid biomethane project in collaboration with Yorkshire Water.
- Approval to publish our inaugural TCFD report.
- Investment in third-party partnerships with strong Board support.
- Approved further investment into SGN's hydrogen (H100) project.
- Agreement to SGN's community support plan for winter 2022.

Suppliers, contractors and partners

We're supported by a significant number of suppliers and contractors to keep our customers safe and warm, while our joint venture partners enable us to develop new technologies and alternative heat solutions.

Why we engage

Our suppliers, contractors and partners play a critical role in enabling us to deliver a safe and efficient service and collectively reduce our environmental impact.

How we engage

- Operational contractor roadshows.
- Supplier checkpoint review meetings.
- Supplier Relationship Management (SRM) programme.
- Sustainability Supply Chain School.

Stakeholder issues raised

- The conclusion of existing contracts including fleet and IT services.
- Contractors' and suppliers' ability to provide ESG-related information.
- Resourcing crisis – recruitment and retention.

Outcomes of engagement on key decisions

- The development and launch of SGN's Sustainable Procurement Code has introduced a new requirement for suppliers we contract with to adhere to the code, including greater provision of ESG-related data and information.
- Introduction of a new fleet framework contract approved for provision of operational vehicles.
- Development of SGN's Safety Improvement Plan which includes active engagement with the supply chain in setting clear health and safety expectations.

Key Board decisions

- Approval of Modern Slavery Statement.
- Approval of new fleet service providers.
- Approval of a new supplier for the delivery of Service Desk, End User Computer and IT Service Management processes.
- Support for suppliers delivering greater sustainability through procurement and training.

Shareholders and debt investors

We have a solid shareholder base, made up of large infrastructure and pension funds, and a large and diverse debt investor base across public bonds, private placements and bank lending.

Why we engage

Understanding our shareholders' and debt investors' needs helps us access a cost-effective, stable, diversified financing base for the business. This also ensures we have access to low-cost debt and equity capital to support growth, which delivers long-term value for existing and future customers.

How we engage

- Annual General Meeting (AGM).
- Board representation and dedicated sub-committees.
- Regular and ad hoc bilateral meetings with shareholders and debt investors.
- Annual results presentations for debt investors.
- Regular and ad hoc meetings with our three rating agencies.

Stakeholder issues raised

- Delivery of Energy Futures initiatives.
- Driving 'best-in-class' safety performance for employees and customers.
- Stable, risk-adjusted investment returns for shareholders and debt holders.
- Continued efficient investment.

Outcomes of engagement on key decisions

- 2022 AGM attended by the Board with new shareholders. All resolutions were passed.
- New Board Director appointments.
- Awareness that the priorities and strategic imperatives of shareholders will not all be the same. The Board aims to understand the views of shareholders and to act fairly as between members of the Group.
- Dedicated strategy sessions for Energy Futures, RIIO-GD3 and annual safety review were held.
- Liaising with shareholders to discuss SGN's ESG and TCFD strategy.

Key Board decisions

- Approved H100 Energy Futures investment.
- Approved the additional resourcing plan.
- Targeting stable credit ratings.
- Formation of the Nomination Committee.
- Appointment of key Executives to drive strategy and the Company vision.
- Dividend payment.
- Support and engagement with SGN's approach to the TCFD reporting requirements.

Engaging with SGN stakeholders

Section 172(1) statement

Section 172(1) of the Companies Act 2006 requires a Director of a Company to act in the way they consider, in good faith, would most likely promote the success of the Company for the benefit of its members as a whole.

In doing so Section 172(1) requires a Director to have regard (among other matters) to:

a. The likely consequences of any decisions in the long term.
b. The interests of the Company's employees.
c. The need to foster the Company's business relationships with suppliers, customers and others.
d. The impact of the Company's operations on the community and environment.
e. The desirability of the Company to maintain a reputation for high standards of business conduct.
f. The need to act fairly between members of the Company.

In discharging their Section 172 duty, the Directors of the Company have regard to the factors set out above. We acknowledge that every decision the Board makes will not necessarily result in a positive outcome for all of our stakeholders.

During the period, the Directors received information to help them understand the interests and views of the Company's key stakeholders and other relevant factors when making decisions. This information was distributed in a range of different formats including in reports and presentations on our financial and operational performance, non-financial KPIs, risk and the outcomes of specific pieces of engagement (for example, the results of customer and supplier surveys and focus groups).

As a result of this, the Directors have had an overview of engagement with stakeholders and other relevant factors which allows them to understand the nature of the stakeholders' concerns and to comply with their Section 172 duty to promote the success of the Company.

On the following page, we have set out an example of how the Directors have had regard to the matters set out in Section 172(1) (a) to (f) when discharging their Section 172 duty and the effect of those on decisions taken by them.

Further details on how the SGN Board operates and how it reaches decisions, including some of the matters discussed and debated during the year, are detailed in this section and on pages 28 to 31.

Key to Section 172 Factors

Long-term impact
The likely consequence of any decision in the long term

Impact on employees
The interest of the Company's employees

Nurturing business relationships
The need to foster the Company's business relationships with suppliers, customers and others

Impact on community and environment
The impact of the Company's operations on the community and the environment

Enhanced corporate reputation
The desirability of the Company to maintain a reputation for high standards of business conduct

Acting fairly between members
The need to act fairly between members of the Company

Board decision

Supporting the development of SGN's future of Energy strategy and continued investment

Section 172 Factors	Directors' consideration of Section 172 Factors
Long-term impact	The UK Government plans for decarbonisation of heat in order to achieve net zero by 2050, and 2045 in Scotland. This presents both an opportunity for SGN to be influential in shaping the future of energy and a challenge. SGN must be able to articulate and execute a robust strategy based on a comprehensive analysis and evaluation of the strategic options in context of likely future states. Establishing a strategic approach and continuing to invest in the future of energy/decarbonisation pathway to achieve net zero will help transition the business to provide a clean energy experience which is key to SGN's vision. Further information on SGN's journey to net zero can be found on page 13 and 'Future of our Network' risk can be found on page 40.
Impact on employees	SGN is committed to providing job security for our colleagues during the energy transition and beyond. In order to do so, SGN continues to work toward proving the viability of future of energy associated projects. To further ensure the success of the strategic approach and keeping our people in mind, SGN provides regular updates on the progress of projects and developments to ensure our people are kept informed and actively encouraged to provide any feedback. More information on how we engage with our people can be found on page 25.
Nurturing business relationships	SGN continues to collaborate and work alongside industry peers, the government, local authorities and Ofgem to support and participate in the development of the UK's pathway to decarbonisation which includes developing pioneering clean energy projects to help shape the UK's future.
Impact on community and environment	The UK's biggest net-zero challenge is decarbonising our homes and buildings. It's the second biggest emitting sector with around 30% of our national emissions coming from around 25 million homes which are connected to gas networks across the UK. The decarbonisation of homes will impact our communities, customers and environment. Customer research helps SGN to understand what matters most to our end-users. Our policy and political work linked to our strategy will amplify our hydrogen demonstration projects and establish as the clear and cost-effective pathway to decarbonise heat at lower cost and disruption to end-users, at pace and scale. Further information regarding SGN's H100 Fife project can be found on page 14.
Enhanced corporate reputation	SGN continues to create the political space to ensure hydrogen is an option in the UK's energy transition and alongside this, that the Company's reputation is strengthened as a world-leading network in the transition for natural gas to hydrogen.
Acting fairly between members	SGN has three supportive shareholders with each having nominated representation on the Board. The Board seeks to always act fairly between shareholders and treat them equally, including ensuring that adequate procedures are in place to address any conflicts of interests that could arise and ensuring equal access to information. With this in consideration, the SGN's Board acknowledges the support from its members and also support the ongoing development of the future of energy strategy to support our customers, the community, and the Government's plans in reaching net zero and longevity of the business.

Engaging with SGN stakeholders

Board decision

Approval of continuing investment in our Cyber Security Programme

Section 172 Factors	Directors' consideration of Section 172 Factors
Long-term impact	The UK National Cyber Security Strategy 2016-21 identified that cyber attacks are growing more frequent, sophisticated and damaging. SGN, along with UK Government and Ofgem, recognises the scale of the cyber threat to critical national infrastructure, such as our gas networks. By not investing in our cyber resilience, we would put our Company at risk of attacks from national states, hacktivists, criminals and/or insiders. Investment is required to ensure our continued cyber resilience against ever-growing threats.
Impact on employees	To maximise the effectiveness of our cyber security programme, we continue to raise employee awareness of cyber risks, and how to protect employees and our Company against cyber threats through training and awareness campaigns.
Nurturing business relationships	SGN continues to work with industry peers and government agencies to ensure our cyber security programme is robust and complies with relevant directives. The Company also receives learnings and best practice from its shareholders' portfolio companies. Following Russia's attack on Ukraine, the National Cyber Security Centre called on UK organisations (including SGN) to bolster their online defences. Ofgem has also provided a Cyber Resilience briefing to the Company and its Board of Directors. The continued investment allows SGN to deliver on stakeholder expectations.
Impact on community and environment	An extreme cyber event could prevent us from distributing gas to our 5.9 million customers. Investment is essential to ensure our cyber defence continues to adapt and improve to the ever-evolving cyber threat landscape, as well as to minimise the risk and impact of cyber events on our core business.
Enhanced corporate reputation	We must invest in our cyber resilience through the cyber security programme to give us the best chance of mitigating the threat of attacks. An attack on our systems that impacts our ability to keep our customers safe and warm could have a catastrophic impact on our corporate reputation.
Acting fairly between members	SGN's shareholders and the Executive management team fully support the decision to continue investing in cyber security.

Board decision

Decision to accept Northern Ireland Utility Regulators GD23 Final Determination for SGN Natural Gas Limited

Section 172 Factors	Directors' consideration of Section 172 Factors
Long-term impact	In determining whether to accept the GD23 Final Determination, the Directors considered the long-term impact the final determination and supporting licence modifications would have on SGN Natural Gas Limited. Taking into account the full determination, including allowances and all modifications, Directors considered it would be in the long-term interest to accept the overall package.
Impact on employees Nurturing business relationships	Directors considered the impact any appeal would have on employees and wider business relationships when considering whether or not to appeal or accept the final determination.
Impact on community and environment Enhanced corporate reputation	Directors considered whether the final determination was in the best interest of each of its stakeholder group and the wider community. In doing so, Directors considered the impact any appeal would have on the deliverability of the licence requirements.
Acting fairly between members	All shareholders were consulted and supported the decision to accept the GD23 final determination.

SGN financial and operational KPIs

We measure our success in achieving our objectives through the use of quantitative and qualitative assessments.

Our key performance indicators (KPIs), which are used to assess the Group's performance, are set out below.

Financial

Cash flow after investing activities[1]

Cash flow after investing activities is the operating cash flow (excluding interest paid) of the business after investment in fixed assets, including both replacement expenditure and capital expenditure. More detail is provided in the consolidated cash flow statement.

2023 **£299.5m**

2022 **£205.0m**

2021 **£417.3m**

Net debt to Regulated Asset Value (RAV) ratio[1]

RAV is defined by our regulators and consists of the RAV of the regulated entities in the Group. Net debt excludes shareholders' loans and liabilities arising from derivative financial instruments and is net of cash and cash equivalents. The percentages stated are as at 31 March. The definitions of consolidated MidCo group and regulated businesses can be found in the ownership structure on page 37.

Consolidated MidCo group

2023 **71.0%**

2022 **75.6%**

2021 **77.4%**

Regulated businesses

2023 **64.5%**

2022 **68.8%**

2021 **70.9%**

[1] Defined in Alternative Performance Measures (APMs) on page 125.

Turnover

Group turnover includes income from the regulated business through regulator price mechanisms and non-regulated income through our commercial activities.

2023 **£1,288.5m**

2022 **£1,115.9m**

2021 **£1,227.4m**

Operating profit

Group operating profit is the net of turnover (above) less the costs of operating the distribution network together with depreciation and amortisation, see note 4 of the financial statements

2023 **£439.5m**

2022 **£364.3m**

2021 **£526.5m**

Capital expenditure[1]

Additions to tangible fixed assets include new distribution mains and storage, new connections to existing mains, new governors and meters, new investment in IT, land and buildings, and vehicles and plant.

2023 **£152.7m**

2022 **£119.9m**

2021 **£127.4m**

Replacement expenditure[1]

Replacement expenditure represents the investment in renewing sections of gas network with modern polyethylene pipes to improve future safety and reliability.

The sections replaced include mains and smaller diameter service pipes, which connect customers to mains.

2023 **£256.7m**

2022 **£229.2m**

2021 **£242.9m**

The sum of capital expenditure and replacement expenditure equal the total additions of intangible and tangible fixed assets as reported in notes 13 and 14 of the financial statements respectively.

Operational

Employee lost time incidents

This is defined as the number of incidents per 100,000 hours worked that result in employees taking time off work. This is one of the key operational metrics that is monitored on a consistent basis. Safety is one of our core Company values and is monitored closely by the Board.

2023 **0.07**

2022 **0.06**

2021 **0.06**

Gas escape attendance

This represents the proportion of uncontrolled gas escapes attended within one hour (target 97%). Uncontrolled gas escapes are defined as those where the smell of gas persists and where the gas supply is still 'on' at the time the customer calls. We responded to over 126,400 uncontrolled and 58,400 controlled gas escapes during the year ending 31 March 2023.

Scotland Gas Networks

2023 **97.2%**

2022 **98.1%**

2021 **99.0%**

Southern Gas Networks

2023 **91.8%**

2022 **97.9%**

2021 **98.9%**

Customer satisfaction (score out of 10): planned interruptions

Results from customer satisfaction surveys (10 = very satisfied). Planned interruptions on our replacement, capital or routine maintenance works are where timing can be predicted and the customer has been notified in advance.

2023 **9.0**

2022 **9.1**

2021 **9.0**

Customer satisfaction (score out of 10): unplanned interruptions

Results from customer satisfaction surveys (10 = very satisfied). Unplanned interruptions arise through leakage or other emergencies.

2023 **9.5**

2022 **9.4**

2021 **9.6**

Customer complaint volume change

This represents the year-on-year increase/(decrease) in complaints expressed as a percentage. Complaint means any expression of dissatisfaction related to any areas of our operation.

2023 **48.3%**

2022 **29.0%**

2021 **(39)%**

Business carbon footprint

Our business carbon footprint includes Scope 1, 2 and 3 emissions, excluding shrinkage, reported in tonnes of CO_2e. This is an absolute number and therefore shows an increase as we are capturing more Scope 3 data than the previous year. Further details can be found on page 51.

2023 **51,161 tCO_2e**

2022 **41,677 tCO_2e**

2021 **24,430 tCO_2e**

Financial review

We continue to prioritise our commitment to deliver safe and efficient networks. During the year we invested over £400m in our networks.

Replacement expenditure*

2023 **£256.7m**

2022 **£229.2m**

2021 **£242.9m**

Capital expenditure

2023 **£152.7m**

2022 **£119.9m**

2021 **£127.4m**

Regulatory asset value*

2023 **£6.97bn**

2022 **£6.38bn**

2021 **£6.00bn**

* Defined in Alternative Performance Measures (APMs) on page 125.

Financial overview

SGN has faced a number of challenges in the second year of the RIIO-GD2 regulatory period, which has impacted the Group's financial performance for 2022/23.

The biggest challenge the Group faced in the year was resourcing, particularly in the south of England. This was due to an increase in churn following the Covid-19 pandemic and adverse market factors, such as labour shortage, making it a constant challenge to recruit and retain talent. The resourcing challenge has made it difficult to meet our emergency response standards during periods of high call volumes, and has required a diversion of engineers away from replacement and connections jobs to support these efforts.

We continue to prioritise our commitment to deliver a safe and efficient network for our customers. During the year we invested £409.4m (2022: £349.1m) in our networks as part of an overall forecast investment of £2.2bn over the five year regulatory price control period. For further details see the 'Investment and safety' section below.

The increase in wholesale gas prices had a significant impact on our industry and our customers. The past 18 months have seen a number of gas suppliers cease trading. When a supplier fails, Ofgem appoints a Supplier of Last Resort (SoLR) to ensure the continued flow of gas to affected customers. The appointed SoLR is entitled to make a claim to cover costs incurred in taking on these additional customers. Under the terms of our licence, these claims are allocated across the gas distribution networks (including Southern Gas Networks plc and Scotland Gas Networks plc) and paid to the SoLR over the subsequent financial year. These payments are made in parallel to the receipt of additional compensating income through the transportation tariffs. SGN received claims of £223.2m which is included within the charges raised to shippers and paid onto SoLRs in the financial year. During the year SGN also received claims of £60.8m which will be raised and paid in the 2024 financial year. We continue to work collaboratively with Ofgem to support suppliers and shippers to ensure the continuity of gas supply to customers.

As a result of the cost-of-living crisis, SGN has partnered with charities and set up community schemes to support our vulnerable customers with their energy bills, pledging £500,000 in the year to support these causes.

Replacing fossil fuels with green alternatives is the most pressing challenge facing the UK's energy system. Almost 85% of UK households use natural gas for heating, so adapting our existing networks to use hydrogen will allow us to decarbonise faster and further than the alternative. In 2022/23, we continued to invest in the future of our networks; advancing our work on net-zero initiatives including our pioneering H100 hydrogen project in Fife, and expanding our biomethane distribution through investment in biomethane plants.

In line with the Group's business plan, we have continued to maximise opportunities in our unregulated businesses, selling and developing some of the redundant brownfield sites held within the SGN Place Group. 2022/23 has seen the sale of a number of surplus gasholder sites for example in Chichester and Farnborough. The SGN Place Group also continues to seek opportunities to develop other key sites through joint venture arrangements.

Investment and safety

Our balance sheet is dominated by our tangible fixed assets and associated borrowings used to fund our capital investment programme. Capital investment for the year amounted to £409.4m (2022: £349.1m), which comprised replacement and other capital expenditure.

Replacement expenditure, primarily associated with the ongoing replacement of mostly cast-iron pipes with polyethylene pipes, totalled £256.7m (2022: £229.2m). The increase in value was due to a rise in contractor rates. These replacement works resulted in 831km of metal pipes being replaced (2022: 849km).

This financial year, due to resourcing constraints, our replacement works focused mainly on the key risk areas. We have worked hard to complete these jobs in a timely manner to minimise the impact on our customers.

Other capital expenditure (excluding replacement) increased to £152.7m (2022: £119.9m). This resulted from the phasing of spend over the RIIO-GD2 period.

Our total RAV for Southern Gas Networks plc and Scotland Gas Networks plc (GB Network) increased by 9.2% in the year from £6.38bn to £6.97bn. The RAV of our GB Network is determined by Ofgem through periodic reviews and is adjusted for sharing of out/underperformance against allowances and inflation indexation. Similar methods are used by the Northern Ireland Authority Utility Regulation (NIAUR) to determine the RAV of our network in Northern Ireland, which was £37.9m at the regulatory reporting date of 31 December 2022.

Treasury and financial risk management

Net debt and leverage

A key financial performance indicator for the Group is the net debt to RAV ratio, which the Group monitors at both an individual network level and at a consolidated MidCo group level. At 31 March 2023, net debt excluding amortised issue costs, shareholder loans and liabilities arising from derivative financial instruments, amounted to:

- MidCo group: £4.95bn (2022: £4.82bn)
- Southern: £3.10bn (2022: £3.01bn)
- Scotland: £1.39bn (2022: £1.38bn)

With RAV at:

- MidCo group: £6.97bn (2022: £6.38bn)
- Southern: £4.79bn (2022: £4.39bn)
- Scotland: £2.18bn (2022: £1.99bn)

The net debt to RAV ratios were:

- MidCo group: 71.0% (2022: 75.6%)
- Southern: 64.8% (2022: 68.5%)
- Scotland: 63.8% (2022: 69.5%)

Covenants

The Group is bound by specific financial covenants with regards to its debt agreements and banking facilities. These are:

- Net debt to RAV ratio (95% for Midco Group, Southern and Scotland)
- Interest cover ratio (1.5:1.0 for Midco Group, Southern and Scotland)

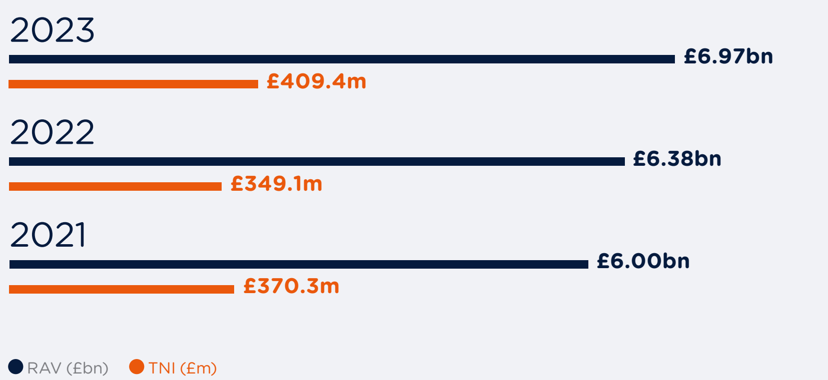
Management assessed the above at 31 March 2023 and consider a breach of these covenants to be remote.

Debt issuance

During the financial year Scotland had a £278.7m RPI-linked public bond that matured in October 2022. The maturity was part-refinanced by a £100m CPI-linked loan put in place in March 2022, which was drawn in September 2022, with the remainder refinanced by £184m of fixed rate private placement notes issued in October 2022. £154m of this issuance was drawn in October 2022 with £30m drawn in March 2023. Other than repaying a £30m drawing on its RCF in April 2022, Southern Gas Networks plc had no debt maturities during the financial year.

In the coming financial year, Southern has a £300m fixed rate public bond maturing in October 2023. To part-refinance this, $132m (£116m equivalent when swapped) of fixed rate private placement notes were issued in October 2022, which were fully drawn in March 2023. Southern put in place additional short-term committed liquidity in June 2023, and further long-term financing will be sought ahead of the October 2023 maturity. Scotland and MidCo have no scheduled debt maturities in the coming year.

Regulatory Asset Value (RAV) and Total Network Investment (TNI)



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Financial review

Turnover

2023 £1,288.5m

2022 **£1,115.9m**

2021 **£1,227.4m**

Cash flow after investing activities

2023 £299.5m

2022 **£205.0m**

2021 **£417.3m**

Operating profit

2023 £439.5m

2022 **£364.3m**

2021 **£526.5m**

For a detailed list of the committed financing that we have in place see notes 19 and 20 to the financial statements.

At the year end, the revolving credit facilities in place for Southern and Scotland were undrawn (2022: £30m drawn at Southern).

The debt service reserve liquidity facility held at SGN MidCo Ltd remained undrawn throughout the year and was extended for a further 364 days to 10 January 2024.

Liquidity

As at 31 March 2023, liquidity within the Group was provided by a combination of cash and cash equivalents and committed bank facilities. The cash balances (held on current accounts or within bank deposits or money market funds) totalled £289.2m (2022: £122.6m) across the Group (of which £41.4m (2022: £25.5m) was restricted cash); and committed revolving credit facilities totalled £360m, all of which was undrawn as at 31 March 2023 (2022: £30m drawn).

In June 2023, a £550m committed bridge facility was signed for Southern in order to provide additional liquidity for its upcoming refinancing activities.

Net finance costs

The Group had net finance costs, including accretion on inflation-linked debt and derivatives, of £336.8m during the financial year (2022: £230m) excluding interest on shareholder loans, interest relating to the defined benefit pension scheme and movement in the fair value of derivatives. This was primarily comprised of interest on external financing arrangements:

- Scotland Gas Networks plc – interest payable £86.3m (2022: £69m)
- Southern Gas Networks plc – interest payable £153.9m (2022: £104m)
- SGN MidCo Ltd – interest payable £28.2m (2022: £21m)

The Group's effective interest rate (including accretion on inflation-linked liabilities and shareholder loan interest but excluding derivative fair value movements) for the year was 5.7% (2022: 5.1%).

The Group's effective cash cost of interest (excluding accretion on inflation-linked liabilities) was 3.2% (2022: 3.9%).

The increase in net interest noted above predominantly reflects the impact of higher inflation on inflation-linked liabilities. The increase in the Group's effective cash cost of interest reflected the prepayment of certain financial guarantees (as further detailed in note 9 of the financial statements).

Risk management

During the year the Group had £278.7m in inflation-linked instruments maturing. As part of the private placement financing activity completed in October 2022, the following interest rate risk and currency risk management activity was undertaken during the financial year:

- In October 2022, Scotland entered into £90m of receive fixed, pay floating interest rate swaps to convert the economics of part of the debt issuance in October 2022 from fixed to floating rates.
- In February 2023, Scotland entered into £30m of pay fixed, receive floating interest rate swaps to re-fix and offset a portion of the £90m swaps referred to above.
- In October 2022, Southern entered into $132m (£116m equivalent) of cross-currency swaps to fully convert the US Dollar principal and interest payments into Pound Sterling on Southern's debt issuance from October 2022.

More details of these instruments can be found in note 21 to the financial statements.

As at 31 March 2023, the gross debt exposure to fixed interest rates (post derivatives) within the Group was:

- Group (consolidated): 58.6% (including shareholder loans) (2022: 57.4%)
- SGN MidCo Ltd (consolidated): 55.8% (2022: 54.2%)
- Scotland Gas Networks plc: 59.1% (2022: 52.9%)
- Southern Gas Networks plc: 53.1% (2022: 52.9%)

As at 31 March 2023 the gross debt exposure to inflation (post derivatives) within the Group was:

- Group (consolidated): 33.7% (including shareholder loans) (2022: 35.1%)
- SGN MidCo Ltd (consolidated): 36.0% (2022: 37.7%)
- Scotland Gas Networks plc: 32.4% (2022: 42.4%)
- Southern Gas Networks plc: 37.7% (2022: 36.2%)

The majority of the inflation-linked debt has an RPI-base apart from the loans raised in March 2022 which has a CPI base. All inflation-linked swaps have a CPI base.

The remaining gross debt exposure was in floating interest rates.

For a more detailed explanation of the Group's approach to risk management see note 21 to the financial statements.

Credit ratings

Of the Group's entities that have external debt financing, two carry public credit ratings: Southern Gas Networks plc and Scotland Gas Networks plc. Each is rated by the same three rating agencies with the following rating (and outlook) applied to the debt raised within those entities at 31 March 2023:

- BBB+ (stable) Fitch
- Baa1 (stable) Moody's
- BBB (stable) Standard & Poor's

During the financial year the following credit rating actions were taken by the credit rating agencies on the Group's public credit ratings:

- 9 June 2022, S&P issued a research update re-affirming the issuer credit rating of both Southern Gas Networks plc and Scotland Gas Networks plc debt instruments at BBB, and maintained their stable outlook.

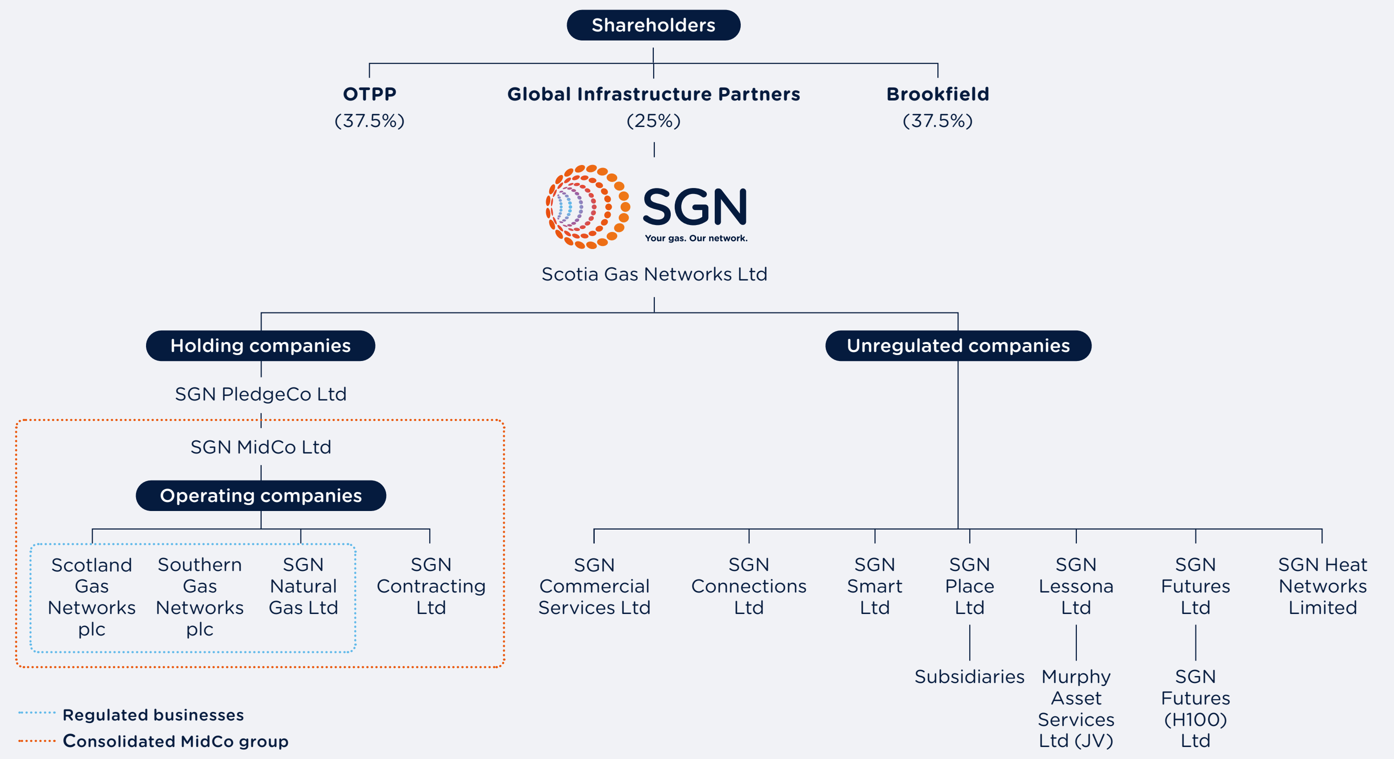
Post the end of the financial year the following credit rating actions have been taken by the credit rating agencies on the Group's public credit ratings:

On 23 May 2023, Moody's issued a research update re-affirming the issuer credit rating of both Southern Gas Networks plc's and Scotland Gas Networks plc's public debt instruments at Baa1, and maintained their stable outlook.

On 26 June 2023, S&P issued an update reaffirming the ratings of

Ownership structure

SGN has three supportive shareholders in place. 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.



Further details regarding the shareholding entities can be found on page 123, note 29.

Financial review

Southern Gas Networks plc and Scotland Gas Networks plc at BBB, and maintained their stable outlook.

The latest credit ratings and reports/publications from each of the credit rating agencies can be found on the debt investor relations section of the SGN website.

Distributions

Our dividend policy across the Group 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 across the Group as well as the Group's financial covenants and credit metrics and targets set by the Board. The inherent risk in the business and wider economy is also considered.

During the financial year Scotia Gas Networks Ltd paid scheduled shareholder loan interest distributions totalling £30.6m (2022: £30.7m). A dividend distribution of £54.5m was paid in November 2022 (2022: £84.0m). No further dividends were declared for 2022/23. At 31 March 2023 Scotia Gas Networks Ltd had £675.5m (2022: £722.6m) of available distributable reserves.

Turnover

The majority of our revenue, 93.3% (2022: 91.7%), is derived from charges to gas shippers for transporting gas through our network, at prices set by Ofgem, our Regulator. During the year, turnover increased to £1,288.5m from £1,115.9m. This is predominantly driven by an increase in our regulated revenue in line with the profile set out within our price control.

Operating profit

Operating profit increased year on year from £364.3m to £439.5m. This is largely driven by the increase in turnover noted previously, and partially offset by increased operational costs linked to resourcing difficulties and additional costs incurred in supporting the emergency response efforts.

Taxation

The current tax rate for the year is 19% (2022: 19%), and the effective tax rate is 37% (2022: 23% (after removing the impact of deferred tax adjustment due to the rise in the main UK corporation tax rate)). The effective tax rate is higher than the standard rate of 19%, the reasons for which are detailed in note 10 to the financial statements.

The Group recognises all tax liabilities which are expected to arise, and only recognises tax assets on uncertain tax positions once the matter has been agreed with HMRC.

Our tax strategy

We shall organise ourselves to ensure that we:

- Comply with all tax legislation requirements.
- Operate within the law.
- Maintain strong relationships with the tax authorities built on trust and co-operation.

Compliance

We are proud to pay our fair share of tax, and our primary objective from a tax perspective is to be compliant with all tax legislation requirements. This includes making timely and accurate returns which reflect our fiscal obligation to government whilst, at the same time, recognising all legislative concessions and reliefs.

Operate within the law

We strive to minimise our total tax liability within the framework of legislative reliefs but do not take an aggressive stance in our interpretation of tax legislation. Our policy is to operate within the law at all times, therefore we do not use artificial tax avoidance schemes or tax havens to reduce our tax liabilities.

Trust and co-operation

Central to our Tax Policy is the maintenance and development of a strong working relationship with HMRC and other Treasury departments based on trust and co-operation.

Tax contribution

Our contribution in relation to UK taxes borne and collected in the year amounted to £416.4m (2022: £371.9m), these consist of the following contributions:

- Corporation tax of £41.6m (2022: £38.3m) paid on our taxable profits
- VAT of £177.1m (2022: £146.5m)
- Business rates of £122.2m (2022: £121.9m) paid to local authorities
- Employment taxes of £75.5m (2022: £65.2m) paid to the Exchequer under PAYE (Pay As You Earn) and National Insurance contributions

Pension commitments

We operate pension arrangements on behalf of our employees. A proportion of our employees are members of a defined benefit pensions scheme, the Scotia Gas Networks Pension Scheme, which was closed to new entrants in 2002. Membership of the defined contribution scheme is offered to all new employees.

In accordance with FRS 102, our balance sheet accounts for any pension asset or liability. As of 31 March 2023, the defined benefit pension surplus decreased from the previous year by £116.5m to £246.0m (2022: £362.5m). The year on year movement was largely driven by a significant increase in AA corporate bond yields, which leads to a higher discount rate and therefore a lower value of liabilities; this has been offset to some extent by high short-term price inflation increasing benefits. There has also been a significant decrease in the value of scheme assets as a result of the negative impact on LDI funds of increasing yields as well as adverse market movements across the year.

The Group contributed £7.7m to the scheme in the year (2022: £20.9m). The Actuarial Valuation report as at 31 March 2021, signed off in March 2022, revealed a surplus and deficit reduction contributions ceased as a result. See note 28 to the financial statements for further details.

Mick Carmedy
Chief Financial Officer
27 July 2023

Principal risks and uncertainties

The aim of our enterprise risk framework is to enable a consistent approach to how we identify, assess, manage, and monitor risks and uncertainties to the successful delivery of our strategic and operational objectives.

Enhancing our risk framework

In 2022/23 we partnered with a specialist provider to conduct a risk maturity assessment and have commenced a programme of work supported by them to reach the next level of maturity, in service of achieving our future strategic and operational objectives. Our 2023/24 Annual Report will provide further detail on this.

SGN principal risks

Our current principal risk profile consists of 12 risks, which are covered below. To ensure SGN focuses on the right risks as we work to build a thriving and enduring SGN, our principal risks are to be fully reassessed (and our associated risk appetite considered) in the first half of 2023/24 by the Executive Committee and Board.

Roles and responsibilities

1	2	3	4
Customer, asset, safety and corporate leadership	Risk and Resilience Committee	Executive Team	Board

1. Business Unit Leadership are responsible for identifying, responding to, monitoring and assuring key risks. Business Units are supported by the Risk function.
2. Our Risk and Resilience Committee includes representation from all parts of the business with a mixture of the Executive team and Senior Leadership. The Risk and Resilience Committee supports the Executive team by overseeing the operational risk registers and making recommendations. It meets quarterly to review SGN's current and future risk profile and resilience capabilities.
3. The Executive owns and oversees the enterprise risk management framework. Each principal risk is assigned an Executive risk owner who is responsible for monitoring the exposure and nature of the risk, deciding how it should be managed and taking the necessary action to bring it back to the desired target level. The Executive receives formal updates following the Risk and Resilience Committee and are supported by the risk function to ensure ongoing risk management.
4. The Board has overall responsibility for making sure that we manage risk within acceptable limits. Our most significant risks are reported to the Board on a bi-monthly basis by our CEO and semi-annually the Board carries out a review of the full principal risk register. The Board is supported by the Audit Committee, who oversees internal controls within the Company. The Board also considers new or emerging risks and recommends ways to tackle them.

Current principal risks

Risk	Key mitigations
Safety & Health	• Health and Safety is our number one priority, and we continue to focus on SGN's safety culture. • Continued focus on safety across all assets and operations, including any changes related to a transition to hydrogen. • Track a range of safety metrics very closely and have programmes in place to drive improvements. • Review lessons learnt from major incidents in order to prevent such things from recurring. • Compliance is supported by independent inspections and an audit programme. • Run wellbeing programmes and campaigns for our people. • Emphasis on leading indicators.
Cyber & IT Resilience	• Cyber security investment programme in place and funding requests made for next stage of the programme. • Increased in-house security team and enhanced managed security service. • Compliance with the Network and Information Systems (NIS) Regulation. • Ongoing work to maintain and improve business continuity and disaster recovery procedures. • Hardware and network resilience/segmentation in place. • Maintenance plan and activities in place to manage the risk of IT failure. • Raising staff security awareness through regular training and awareness campaigns. • Participation in audits and exchanges on learnings and best practices.
Licence Conditions	• Governance and compliance frameworks to deal with issues and developments arising from price controls. • Experienced regulation, finance and legal teams. • Engage with all levels of Ofgem and government. • Delivery of regulatory outputs is measured and monitored on a regular basis. • Annual Compliance Report. • Improved data analytics and predictive models including to inform resourcing requirements.

Principal risks and uncertainties

Current principal risks (cont)

Risk	Key mitigations
Leadership, People & Culture	• Training and development including talent management programmes, which are being reviewed to ensure future fit. • Recruitment of the required number of operational, front-line employees has been made a Company-wide priority. • Outsourcing of some training to approved suppliers. • Responding to regulatory, supplier and technology developments which may impact on Company strategy. • Three-year pay deal protecting employees against inflationary pressures, plus attract and retain people. • Retrain and recruit in synchrony with the hydrogen transition.
Future of our Network	• Active in influencing government and industry stakeholders to lobby for hydrogen rollout. • Creation of the Strategic Hydrogen Executive with other GDNs. • Delivering SGN evidentiary framework and developing plans for heat decarbonisation rollout. • Utilising innovation funding and working with others to deliver evidence for potential decarbonisation pathways. • Developing plans to develop hydrogen storage and production investment opportunities. • Developing a range of other opportunities, including MUA, biomethane, heat networks.
Financing	• The Group has a treasury policy which aims to maintain: – 12 to 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. – A proportion of direct or synthetic inflation-linked debt liabilities. • Regular internal monitoring and reporting of key credit metrics and financial covenants to the Board. • Annual results presentations intended for debt investors. • A flexible dividend distribution policy linked to maintaining credit metrics.
Political & Public Policy Risk	• Contributing to development of UK and Scottish governments' policy. • Continue to build capability to explain our role and how we contribute to delivery of government policy ambitions. • Targeted engagement with local authorities to develop decarbonisation plans. • Assessment of Scottish independence risk/opportunity to SGN.
Environment & Climate Adaptation	• Delivering the Environmental Action Plan and Environmental Sustainability Strategy. • Engaging with the supply chain to support their journey of decarbonisation and environmental improvement. • Regular interaction with stakeholders and customers including collaboration with SGN Environment Advisory Panel. • Engage with peers and other companies in the energy and infrastructure sectors to enable a best practice approach. • Maintaining our ISO14001:2015 Environmental Management System certification. • Understanding and assessing climate risk to occupied sites and our network. • Pilot projects to demonstrate the safe, efficient and effective transport, storage and use of hydrogen.
Supply Chain	• Developing and harnessing new suppliers to encourage competition, innovation and resilience. • Supplier performance management and compliance across key areas. • New Logistics team in place to prepare for migration of Logistics service from existing MSA provider. • Ongoing support and management of contracts and supply chains. Planning to deal with short and long-term shocks. • Online sourcing and contract management system. • Issued new Sustainable Procurement Code.
Legal & Compliance	• Programmes to strengthen our compliance framework, supported by risk-based training programmes. • Code of Conduct and compliance policies covering controls. • Speak Up (Whistleblowing) Policy. • SGN contracts include compliance clauses. • Training and communications to guide and support our people to meet legal and regulatory requirements. • Ongoing assessments to help manage compliance risks associated with business change/developments. • Annual Compliance Report.
Customer Interests	• Customer Experience RIIO-GD2 project, utilising customer insight to ensure we are meeting customer expectations. • Focused training plans to embed processes and upskill our people to deliver the best. • Vulnerable Customer Strategy to harness new partners and encourage innovation for services and communications. • Ongoing support and management of external relationships to maximise collaboration and co-operation. • Contribute, together with all stakeholders, to the development of a fair and affordable transition.
Network Asset Management & Physical Security	• Clear asset investment strategy out to March 2026. • 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. • Robust annual audit programme and site inspections to ensure compliance with our policies and procedures. • Closely track a range of asset and safety related metrics and have programmes in place to drive improvements. • Test resiliency through several activities such as emergency exercises and risk assessment tools. • A physical security upgrade programme designed to meet government agencies' guidelines. • Learning from incidents within SGN and externally.

TCFD report

Climate change presents financial risk to the global economy. Financial markets require clear, comprehensive, high-quality information on the impacts of climate change.

This includes the risks and opportunities presented by extreme weather events, rising temperatures, climate-related policy, and emerging technologies in our changing world. The Financial Stability Board (FSB) created the Task Force on Climate-related Financial Disclosures (TCFD) to improve and increase reporting of climate-related financial information. As per Companies Act (2006), for companies with >500 employees and >£500m turnover, it is mandatory to report in alignment with TCFD for periods beginning on or after 6 April 2022.

As highlighted in our Environmental, Social and Governance (ESG) report of 2022 we focused our efforts over the last financial year to provide disclosures aligned with the TCFD framework. We are therefore pleased to present our responses to each of the recommended disclosures in the below table and on the following pages. We appreciate that this reporting is part of our sustainability journey, and during this first phase of TCFD reporting, we have identified areas for further development. For additional detailed information on risks, please refer to 3rd Round Climate Change Adaptation Report.

Disclosure recommendation	Alignment with TCFD	Section reference	Page
Governance			
Describe the Board's oversight of climate-related risks and opportunities	Partial	Principal risks and uncertainties TCFD	39-40 42
Describe management's role in assessing and managing climate-related risks and opportunities	Partial	Principal risks and uncertainties TCFD Board Committees hierarchy	39-40 42 60
Strategy			
Describe the climate-related risks and opportunities the organisation has identified over the short, medium and long term	Partial	TCFD	43
Describe the impact of climate risks and opportunities on the organisation's businesses strategy and planning	Partial	TCFD	43
Describe the resilience of the organisation's strategy taking into consideration different climate-related scenarios, including a 2°C or lower scenario	Not included at this stage	TCFD	44
Risk management			
Describe the organisation's processes for identifying and assessing climate-related risks	Partial	Principal risks and uncertainties TCFD	39-40 44
Describe the organisation's processes for managing climate-related risks	Partial	TCFD	44
Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management	Partial	Principal risks and uncertainties TCFD	39-40 44
Metrics and targets			
Disclose the metrics used by the organisation to assess climate-related risk and opportunities in line with its strategy and risk management process	Fully	Streamlined energy and carbon reporting TCFD	51 44
Disclose Scope 1, Scope 2 and, if appropriate, Scope 3 greenhouse gas emissions and the related risks	Fully	Streamlined energy and carbon reporting TCFD	51 44
Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets	Fully	ESG Report TCFD Annual Environmental Report on website	50-51 44

TCFD report

Governance

Board oversight
Our Board has a focus on steering and supervising SGN across strategy, performance, and governance in the short, medium, and long term. This is discussed at each meeting of the Board as appropriate. Disclosure on how the Board considers climate-related issues can be improved.

'Environment and climate adaptations' has been identified as one of the 12 Principal Risks to SGN.

- The Board has oversight of the enterprise risk management system which includes climate-related risks. The Board is responsible for overall risk management strategy, with responsibility for management of risks sitting with the relevant managers. Ongoing input is provided by the Executive leadership team giving visibility to the nature and extent of risks facing the organisation.
- Our sub-board committee, the Stakeholder and ESG committee, which is chaired by one of our Non-Executive Directors and Board members, has oversight of environmental risks and opportunities. They meet three times a year. The Chair reports climate-related matters to the Board.
- Climate-related KPIs are being reported at Board level. These metrics are provided as part of the CEO report to the Board at each bi-monthly meeting. Climate-related metrics are also included in the monthly Executive dashboard which is presented to the Board.

Management's role
Our Safety, Health and Environment Policy is signed at Executive Director level and provides an overall framework and principles of action for our approach to managing the impact of our business on the environment. The policy provides a commitment to manage the impacts and aspects of climate change associated with our operations and assets.

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This pipeline washout in Scotland which happened in August 2020 is an example of climate related risk to SGN.

Overall management level responsibility for sustainability, including the strategic risk of climate change, sits with the Director of Stakeholder Relations and Communication and the Head of Sustainability.

Risks are assessed through a comprehensive risk management system and each directorate has its own risk register. Climate-related risk and opportunity management is devolved to the different directorates through the risk registers, where 'environment' is one of the impact measures.

To ensure knowledge is shared throughout the organisation we include climate-related business information and KPIs on a regular basis (monthly) to the Executive team and senior managers.

- Our 'Executive dashboard' includes climate related business information and KPIs. This is shared with all senior managers in the organisation and provided at Executive meetings on a monthly basis.
- Climate related information and metrics are also reported monthly to the Executive team through the Stakeholder Relations and Communications Directorate dashboard.

Strategy

Climate risks and opportunities over time
The process for identifying risks and opportunities was through a series of workshops with key internal stakeholders at senior management level within the organisation. Going forward the process for keeping climate risks and opportunities updated will be further developed by incorporating it into business wide risk management procedures and reporting to the Board on a regular basis.

Our Board has oversight of the enterprise risk management system which includes climate-related risks.

In SGN we are defining short term as the immediate one to two years ahead. Medium term is defined as three to nine years, in line with the next Ofgem price control, and long term is defined as the next 10 to 20 years, in line with our net-zero goal.

Over these time periods we have identified several physical risks, including:

- Weather events that have an impact on the integrity of the network or damage to assets, such as flooding (coastal, fluvial, pluvial and/or groundwater).
  - Whilst many of our assets will function under water for a period of time, the ability to maintain them is critical. Waterlogged ground can have a detrimental effect on the degradation of assets. For example, a pipeline project in Dunkeld, in our Scottish network, was born out of the need to re-route a below-ground pipeline that had been exposed by fluvial flooding due to its close proximity to a river. Physical risks to our assets have been more closely examined and reported on in our 3rd Round Climate Change Adaptation Report.
- Above ground assets, for example governors, are also important to include when preparing physical risk assessments.
- Prolonged heat and cold weather events can impair equipment and impact supply chain, for example ability to access sites.
- Chronic longer-term changes to weather patterns could impact natural gas demand and management of peak demand versus underutilisation of the network.
- Extreme weather events may impact on the health, safety and wellbeing of colleagues, particularly those who are field based.

We have acquired specific data sets which will help us better assess climate risk in particular related to flooding. The following transition risks have been identified:

Policy and regulation
- This is expected to increase over time. Currently the following key risks have been identified:
  - net zero targets for the UK and Scottish governments as per relevant Climate Change Acts;
  - ban on new petrol and diesel vehicles by 2030;
  - potential carbon taxes;
  - emerging regulation on increased sustainability reporting and disclosure.

Market
- Natural gas demand may be impacted by market pressures. Another risk would be around people skills and experience: we will need to ensure we have the right skilled resource to work with emerging decarbonised technology. This in turn adds to competition in the market for the right people with the right skills.
- Government strategic decision on hydrogen in 2026, on how significant a role hydrogen will have in decarbonising domestic heat.

Reputation
- As a gas distribution network, we acknowledge that there are reputational risks in being associated with the fossil fuel industry both in terms of our standing with customers and other stakeholders, such as debt investors and credit rating agencies. However, this is also an opportunity, as SGN can take a leading role in the decarbonisation of the network.

Technology
- Risks identified include the transition towards low carbon heating technologies, including technology utilising green or blue hydrogen. Our Future of Energy team works specifically in this area, as it is also an opportunity for SGN.
- Risks associated with the move to hydrogen include water availability for production.
- Risks are also identified in the transition to a zero emissions fleet and associated costs and availability of the vehicles and charging infrastructure.

Opportunities identified include:

- The energy transition could open up new market opportunities with increased consumer demand for low-carbon heating solutions. With encouraged flexibility and consumer choice in relation to the options available for low carbon energy this could help to secure a just transition to net zero.
- Support for biomethane and hydrogen use in the low carbon transition.
- Change and diversity in revenue mix and sources.
- Aligning with a net-zero strategy may make us a more attractive investment for debt and equity investors.
- Investment in decarbonisation innovation activities including incentives for new technologies.

Impact on businesses strategy and planning
Identified risks and opportunities are raised with the Board and can impact business planning. We assess capability, financial, environmental, safety, reputation, and regulatory impacts and these are defined in our risk register. Significant financial impact is defined as:

- Financial impact between £15m to £50m with an almost certain likelihood i.e. >90%;
- Financial impact between £50m to £100m with a 50% to 90% likelihood; or
- Financial impact of more than £100m with a possible impact of 30% to 50%.

For example, as part of Ofgem's price control, all assets have monetised social and replacement cost linked with losing the asset. This is overlaid with climate-related information (e.g., flooding, heatwaves) for climate related events.

Further development of climate-related risk and opportunities management and incorporation into business strategy and planning including financial planning has been identified and will be an important part in the next phase of strategy development in line with TCFD recommendations.

TCFD report

Scenario planning

We are not yet using climate-related scenario analysis to determine resilience of the organisation. This will be considered in the next phase of strategy development in line with the TCFD recommendations.

Risk management

Processes for identifying and assessing climate-related risks

At an operational level we identify and assess sources of risks, including climate-related risks, through our Environmental Management System. This is achieved through the determination of significant environmental aspects and impacts. We also use different mapping tools, including maps from the Environment Agency and Scottish Environment Protection Agency to identify and assess physical risks to our networks.

At a strategic level our principal risk profile consists of 12 risks reflecting the changing nature of the business environment, political and regulatory environment, price control objectives, strategic objectives and other external risks. Each of the 12 risks are ranked in terms of residual impact (i.e. after mitigating activities) to our business. 'Environment and climate adaptations' has been identified as one of our 12 Principal Risks.

Identifying and assessing the strategic environmental risk to the business is the responsibility of the stakeholder engagement and communications directorate applying the risk impact matrix. Our stakeholder and ESG sub-board committee oversee the risk. Our most significant risks are reported to the Board on a bi-monthly basis by our CEO and semi-annual the Board carries out a review of the full principal risk register. Decarbonisation of the network is at the core of SGN's strategy. Our efforts and work in the Future of Energy is a testimony to this.

Managing climate-related risks

Operational risk registers are owned by each directorate, where they identify the risk and opportunity within their area of the business. They assess and score risks based on a consistent risk assessment framework used across the business, this is then fed into the enterprise risk management system. Issues and actions against risks are recorded, with timelines and responsible people assigned to risks. This is then used as an action plan to address risks.

Integration into overall risk management

The oversight of the enterprise risk management system is Board-led with ongoing input from the Executive leadership team giving visibility to the nature of risks and extent of risks facing the organisation. Oversight of the principal risks (including environment and climate adaptation) remains effective through several established routes during the year. Each principal risk is assigned an Executive owner who is responsible for monitoring the exposure and nature of the risk, deciding how it should be managed and taking the necessary action to bring it back to the desired target level.

Processes are being developed to ensure that specific climate-risk identification is included within the wider risk management process.

Metrics and targets

Metrics

As part of our Environmental Management System, we routinely track progress against our targets to ensure that our approach meets the expectations of our stakeholders and the Regulator. Our Environmental Management System is independently verified through certification to the ISO 14001:2015 standard. We have been certified to ISO 14001 for 18 years.

In our ESG report (pages 50 to 51) we disclose KPIs on our carbon footprint Scope 1, including shrinkage, and Scope 2, as well as metrics on network leakage, and number of biomethane sources.

We have an opportunity to further link our metrics and targets to the relevant climate-related risks and opportunities in line with our business strategy.

Greenhouse gas emissions

The biggest contributor to climate change impact we have is through Scope 1 shrinkage and in particular leakage from the network which is the biggest component. We have an interim 2025 target for our emissions excluding shrinkage, and we are also working to develop an interim target for shrinkage. We have committed to net zero by 2045 for Scope 1, 2 and 3 emissions. In February 2023 we achieved the Carbon Trust Route to Net Zero – Taking Steps accreditation, which acknowledges the emissions reductions and processes we currently have in place to drive change.

Leakage is being reduced through replacing old metal mains with polyethylene pipe, effective pressure management and innovative solutions. Moving towards low carbon energy supply, including the opportunity of hydrogen, would change the emissions profile for SGN, and provides a key risk as well as an exciting opportunity for us.

Targets and performance

We have set a net zero by 2045 target for our operations and networks. We are also working to support the decarbonisation of UK's heat network, see page 13 'The journey to net zero'.

Progress against our greenhouse gas emissions targets and how we are increasing the availability of biomethane in the networks, are set out in the ESG Report. In addition, we have other climate-related targets supporting our environmental strategy, such as developing biodiversity projects to create more healthy green spaces at our sites and depots while also benefitting local communities, aiming to achieve biodiversity net gain. We also engage with and support our suppliers to implement ESG targets and improve their environmental impacts.

For a more comprehensive reporting on what we are doing to meet our environmental strategy, please see the Annual Environmental Report on our website.

Environment, Social and Governance (ESG) report

Laura Sandys
Non-Executive Director and Chair of SGN's Stakeholder and ESG Committee

"2022 was the UK's hottest year on record, with an average temperature of over 10°C recorded for the first time. The unprecedented impacts of climate change require continued mitigation to keep the world aligned with the international Paris Agreement and UK's legislative net-zero target, as well as adaptation to a changing climate. Our work to contribute to reduce the carbon emissions of UK's many homes and businesses that rely on natural gas is increasingly important, as are the efforts to reduce our own asset and operational carbon footprint.

In this Annual Report we are for the first time, responding to the recommendations of the TCFD. This shows how we ensure appropriate governance of climate related risks and opportunities to our business, how we identify, assess and manage these risks and opportunities, how they impact our strategy and how action is monitored. In essence the report shows how climate change is tackled in SGN. As part of our sustainability journey, we have also identified opportunities for further development and improvement.

Our biggest asset is our people. We need to continue to strive to hire the best talent so we can support a just energy transition and provide our customers with the best energy experience. Our ESG report shows how we are making progress and where we need to work harder to make this a reality."

Rob Gray
Director of Stakeholder Relations and Communications

"In a year where the cost-of-living crisis has hit many of our vulnerable customers, we are very pleased that our portfolio of partnerships supported more than 118,500 vulnerable households through our Vulnerability and Carbon Monoxide Allowance (VCMA) initiatives. We have achieved next year's target, already this year with 170,870 households helped to use energy safely, efficiently and affordably. These vulnerable households have accessed over 308,500 unique support services achieving over £14m in social value. We have 51 approved initiatives including SGN's Safe & Warm community scheme which has onboarded 17 grassroot local partners under one collaboration.

We are making great strides on our climate change response. This has been acknowledged in several ways: SGN was featured on the 2022 CDP Supplier Engagement Leader board, being among the top 8% global organisations assessed for supplier engagement on climate change. We have achieved a score of B on our climate change disclosure submission to CDP, which is above the global average for the oil and gas sector. And we achieved the Carbon Trust Route to Net Zero standard, Taking Steps tier, showing our commitment towards a continuous reduction of our carbon footprint and a decarbonised future. We are proud to be leading the way in the energy industry as an early adopter of this new standard."

Environment, Social and Governance (ESG) report

This is the second year we present our ESG report. The reporting is aligned with the World Economic Forum's (WEF) Stakeholder Capitalism Metrics framework and our material aspects.

We believe this is a good way of showing our wider commitment and responding to environmental, social and governance issues pertinent to our business and to our stakeholders. Specifically for this year, we have for the first time included disclosures on our climate-related risks and opportunities, as per the TCFD guidance. This report is part of our Annual Report pages 41 to 44.

On the following pages we disclose performance for financial year 2022/23, in comparison with last year's disclosure and any relevant targets. Where a metric as per the WEF framework is not material to the business, we have explained this. As a business we are also committed to show how we are making progress in supporting the UN's Sustainable Development Goals (SDGs), and therefore we show how the pillars of the WEF framework, and our material issues, link to these important global goals.

Our material issues, are supported by the Sustainable Development Goals, and are as follows:

Principles of Governance

- Delivering an excellent service for customers and stakeholders
- Creating an ESG strategy that reflects and underpins our Company culture

Governance is foundational to achieving long-term value by aligning and driving both financial and societal performance, as well as by ensuring accountability and building legitimacy with stakeholders.

While good governance is important for achieving all of the Sustainable Development Goals, it is highlighted specifically in three of them:

SDG 12
Responsible consumption and production

SDG 16
Peace justice and strong institutions

SDG 17
Partnerships for the goals

We have identified goal number 12 as a high priority to our business and to our stakeholders.

Planet

- Decarbonising the gas grid and innovating to provide our customers with cleaner energy
- Tackling the carbon impact of our business today, including emissions from leakage
- Responding to the physical risks of climate change through adaptation and improvement

Businesses depend on and impact the natural environment in a myriad of ways. At SGN we impact the environment through our operations and supply chains and through the way our networks are used. Our impacts on the environment can result in significant societal harm unless we manage our impacts well and aim to reduce and improve across our business activities.

Six Sustainable Development Goals are particularly relevant to corporate environmental disclosures:

SDG 6
Clean water and sanitation

SDG 7
Affordable and clean energy

SDG 12
Responsible consumption and production

SDG 13
Climate action

SDG 14
Life below water

SDG 15
Life on land

We have identified goal numbers 7, 12 and 13 as high priorities to our business and to our stakeholders.

People

- Making sure SGN is a great and inclusive place to work, where all people thrive and develop careers
- Securing the safety and wellbeing of all customers and colleagues
- Recruiting and retaining a diverse range of talented people excited about shaping the UK's energy future

We are living in a connected world in which society is increasingly committed to the values of responsible business, sustainable economic development and long-term value creation. People are at the front and centre of the Sustainable Development Goals, and also at SGN.

Achievements related to people are strongly linked to all Sustainable Development Goals, and the importance is specifically highlighted in six of them:

SDG 1
No poverty

SDG 3
Good health and wellbeing

SDG 4
Quality education

SDG 5
Gender equality

SDG 8
Decent work and economic growth

SDG 10
Reduced inequalities

We have identified goal numbers 3, 5 and 8 as high priorities to our business and to our stakeholders.

Prosperity

- Creating a sustainable future for our business while providing a safe, reliable and affordable service
- Maintaining an attractive and flourishing business respected by a wide range of stakeholders

Businesses have impacts on, and benefit from, economic and social prosperity in several ways and it is widely recognised that businesses cannot succeed in a failing society. Prosperity is described both in financial terms and through non-financial key performance indicators. Four Sustainable Development Goals have core features of prosperity:

SDG 1
No poverty

SDG 8
Decent work and economic growth

SDG 9
Industry, innovation and infrastructure

SDG 10
Reduced inequalities

We have identified goal numbers 8 and 9 as high priorities to our business and to our stakeholders.

By tackling the priority impacts we have across our networks we are also contributing towards achieving the SDGs.

Environment, Social and Governance (ESG) report

Principles of Governance

Aspect	Non-financial KPI	Target/tracking	2022/23	2021/22	Comment
Delivering an excellent service for customers and stakeholders	Emergency response service – controlled gas escapes	Scotland: 97% regulatory standard	96.6%	99.5%	Our Scotland and Southern networks performed below regulatory standard. We have an action plan in place to ensure Emergency Response KPIs are achieved in the coming year.
		Southern: 97% regulatory standard	92.4%	98.9%	
	Emergency response service – uncontrolled gas escapes	Scotland: 97% regulatory standard	97.17%	98.1%	
		Southern: 97% regulatory standard	91.86%	97.9%	
	Network reliability (as % of full liability)	Scotland: 100%	99.999%	99.999%	Our network remains extremely resilient, with our customers currently experiencing an interruption only once every 50 years on average. We continue to provide excellent customer service and seek ways to further reduce the inconvenience of being without supply.
		Southern: 100%	99.998%	99.999%	
	Gas transported	Tracking	131.8 TWh	138.8 TWh	There has been a drop off in demand due to the increase in wholesale gas prices impacting end users demand usage.
	Customer satisfaction	Scotland: 9	9.30	9.28	Both networks have achieved business case targets of delivering service which is >=9/10 and Scotland continues to retain number one GDN position for the seventh year in a row.
		Southern: 9	9.02	9.03	
	Complaints metric	Scotland tracking	1.71	1.5	Both networks have successfully sustained a score of under 5.00 for Ofgem's complaints metric, which is the penalty threshold. For Scotland's network, 83% of complaints were resolved within day +1 and 100% resolved within day +31. For Southern 57% were resolved within day +1 and 99% in day +31.
		Southern tracking	4.74	3.17	
	Additional services referrals	Tracking	7,083	4,098	We have had a huge increase in customers referred this year due to the engagement throughout the business and the additional services we put in place to support for those most vulnerable during the cost-of-living crisis and awareness raising of customers who should be referred through to priority service register. From the customers referred they have benefitted from over 11,141 services from our partners. The biggest increase in services requested is our Emergency Fuel Top Ups and Food Vouchers, with onward support for energy efficiency advice and income maximisation checks.
>>>>>>	Priority services register	Tracking The referrals includes referrals made through partners	17,153	7,415	

Aspect	Non-financial KPI	Target/tracking	2022/23	2021/22	Comment
Delivering an excellent service for customers and stakeholders (continued)	Fuel poor gas connections	Tracking	649	1,410	This is lower than 2021/22 partly due to the impact of the removal of gas boiler and appliance funding under the Energy Company Obligation, meaning fuel poor households are unable to access support with the costs associated with installing gas central heating systems and boilers.
Creating an ESG strategy that reflects and underpins our Company culture	Setting purpose	We set our purpose in 2021/22: Serving our communities by keeping everyone safe and warm. Pages 6 to 7.			
	Quality of governing body	SGN governance structure, pages 60 to 62. SGN Board roles and responsibilities, pages 63 to 67.			
	Material issues impacting stakeholders	Please refer to our material issues for our ESG reporting on pages 46 to 47 and how we engage with stakeholders on pages 25 to 28.			
	Stakeholder relationship satisfaction	Tracking	8.2	8.1	Relationship satisfaction increased slightly from 8.1 last year, to an all-time high of 8.2 this year.
Ethical behaviour	Anti-corruption, compliance training and awareness sessions	Tracking	14,867	13,432	Across the compliance areas of Privacy, Business Separation, Business Ethics and Modern Slavery we have delivered a total of 14,867 sessions. This is 96% of the planned 15,480 sessions. We have implemented a Code of Conduct this financial year.
	Anti-corruption incidents	We treat the number and proportion of corruption incidents as confidential Company information.			
Protected ethics advice and reporting mechanisms	Speak Up reports	Tracking	44	32	Empowering people to speak up against wrongdoing is a central element of our approach to doing the right thing. This can be done through an independent whistleblowing channel, called Speak Up Hotline, as well as through various internal channels. We promote this mechanism to our people through our Safe to Speak Up campaign. We are working to improve the top three categories of Speak Up issues, namely substance abuse, discrimination/harassment, and safety, health and environment.
Risk and opportunity oversight	Integrating risk and opportunity into business process	Principal risks and uncertainties, pages 39 to 40.			

Planet

Aspect	Non-financial KPI	Target/tracking	2022/23	2021/22	Comment
Decarbonising the gas grid and innovating to provide our customers with cleaner energy	Volume of new biomethane in the network	Tracking	0	1,500 scm/h	This is measured in scm/h, standard cubic metres per hour, meaning standard cubic metre of gas per hour. SGN had a strong year in relation to developing potential new biomethane connections and also managing connections which will connect in 2023/24. Across 2022/23 we have had 103 enquires from biomethane project developers for potential new sites and also 20 detailed capacity studies which points to very buoyant biomethane connections market.
	Growth in biomethane	Tracking Equivalent number of households supplied with biomethane	259,000	259,000	
Tackling the carbon impact of our business today, including emissions from leakage	Greenhouse gas emissions	See our Streamlined energy and carbon reporting (SECR) table on page 51. We have a net zero by 2045 target which includes greenhouse gas Scope 1, 2 and 3. We also have an interim target for Scope 1 and 2, excluding shrinkage, to reduce by 25% by end of financial year 2026. We are developing an interim target for shrinkage.			
Nature loss	Land use and ecological sensitivity				For this metric we have chosen to show how many biodiversity site studies we have completed. Across these sites we are progressing a programme of biodiversity improvements aiming for biodiversity net gain. The suggested WEF measurement of sites adjacent to protected areas or key biodiversity areas is not material to the business.
	– Biodiversity studies completed	Tracking	50	6	
	– Improvement projects	Tracking	6	0	
Conservation of water	Water consumption and withdrawal in water-stressed areas: This metric, part of WEF framework, is not material to our business.				
Responding to the physical risks of climate change through adaptation and improvement	TCFD implementation	Task Force for Climate-related Financial Disclosures (TCFD) report, pages 41 to 44.			

Streamlined energy and carbon reporting

	2022/23	2021/22	% change
Scope 1 and 2 (Direct emissions)			
Scope 1: Gas usage from our occupied/operational sites (tCO_2e)	**3,144**	5,106	-38%
Scope 1: Natural gas shrinkage (Leakage + Theft of Gas + Own use of gas) (tCO_2e)	**696,634**	721,448	-3%
Scope 1: Business mileage Company owned/controlled vehicles (tCO_2e)	**13,667**	17,140	-20%
Scope 2: Purchased electricity (Location based) (tCO_2e)	**2,491**	2,127	+17%
Scope 2: Purchased electricity (Market based) (tCO_2e)	**32**	128	-75%
Total Scope 1 and 2 (tCO_2e)	**715,936**	745,821	-4%
Scope 1 and 2 Energy consumption (kWh)	**691,158,678**	666,885,940	4%
Intensity metric: Total Scope 1 and 2 per £m turnover (tCO_2e/£m)	**579**	667	-13%
Intensity metric: Total Scope 1 and 2 per km gas pipe in network (tCO_2e/km)	**9.9**	10.3	-4%
Intensity metric: Total Scope 1 and 2 per energy throughput (tCO_2e/GWh)	**5.4**	5.3	2%
Scope 2: Purchased electricity (Market based) (tCO_2e)	**32**	128	-75%
Scope 3 (Indirect emissions)			
Business travel (Rail, Air, Ferry, Car Hire, Grey Fleet) (tCO_2e)	**709**	420	+41%

Methodology

Data provided here is in line with annual regulatory reporting of carbon footprint to Ofgem using Defra conversion factors. Greenhouse gas emissions are calculated in alignment with the Greenhouse Gas Protocol, operational control. It includes data from our Southern and Scotland networks. Conversion factors are updated annually. Where market-based factors are stated these are provided annually by our electricity suppliers. Total annual net emissions figure uses market based methodology. Intensity metrics have been agreed with the Energy Networks Association (ENA).

Commentary on changes

Scope 1 gas usage from occupied/operational sites is low this financial year compared to last year. This is due to our single biggest gas consumption item having been off due to maintenance for a period of time, hence generating no emissions.

We are now powering approximately 98% of our offices with certified renewable electricity. This is shown through the very low market based emissions for our Scope 2. We have a programme in place to install direct feed renewables which will reduce our location based emissions Scope 2 over the coming years.

Natural gas shrinkage, Scope 1, which is the biggest contributor to our carbon footprint, is continuing to reduce as we are progressing with our replacement works (replacing old metal main pipes with new polyethylene pipes), effectively managing pressures and reducing gas escapes through innovation.

Our business travel has increased this financial year compared to last, as travel has resumed with lifting Covid-19 restrictions. It is worth noting that our business travel emissions are much lower than they were pre-pandemic. Using technology and video calls have become more embedded in our ways of working.

We know that the biggest impact of our Scope 3 comes from products and services that we procure. We are working towards capturing material Scope 3 categories and provide full disclosure.

Environment, Social and Governance (ESG) report

People

Aspect	Non-financial KPI	Target/tracking	2022/23	2021/22	Comment
Making sure SGN is a great and inclusive place to work, where all people thrive and develop careers	Diversity and inclusion – gender	Tracking	81% Male 19% Female	81.5% Male 18.5% Female	
	Diversity and inclusion – ethnicity	Tracking	86% White 3.6% Ethnic minority 9.6% Data not held	85% White 5% Ethnic minority 10% Data not held	
	Diversity and inclusion – disability	Tracking	8% Yes 38% No 2% Prefer not to say 52% Data not held	7% Yes 37% No 1% Prefer not to say 55% Data not held	
	Diversity and inclusion – age group	Tracking	<1% Under 20 15% 20s 32% 30s 22% 40s 20% 50s 9% 60s <1% 70s	<1% Under 20 17% 20s 29% 30s 23% 40s 21% 50s 9% 60s <1% 70s	
Recruiting and retaining a diverse range of talented people excited about shaping the UK's energy future	Pay equality	Please refer to our Gender Pay Gap report on our website: • Scotland Gas Networks • Southern Gas Networks • SGN Contracting			
	Wage level	We do not have access to robust up-to-date data for gauging local minimum wage that would allow for comparison against our own data and don't anticipate this data will become readily available in the short to medium term. Where necessary and relevant, we benchmark salaries for roles within our organisation using an external consultancy to ensure we are paying a fair market rate. We are a living wage employer.			
	Training provided: Total investment	Tracking	£4.9m	£4.4m	This equates to over £1,200 for each employee per average. The last six months of the year there was a focus on tier 1 training due to pressure and workload demands on our operational business.

Aspect	Non-financial KPI	Target/tracking	2022/23	2021/22	Comment
Securing the safety and wellbeing of all customers and colleagues	Modern slavery training	Training 100% of our workforce by June 2023	3,189	2,757	Across the compliance areas of Privacy, Business Separation, Business Ethics and Modern Slavery we have delivered a total of 14,867 sessions. This is 96% of the planned 15,480 sessions.
	Health and safety – number of fatalities as a result of work related injury	0	0	0	
	Injury rates: total recordable injury rate	0.08	0.13	0.15	Total recordable injury rate is the number of HSE reportable, lost time and medical treatment injuries multiplied by 100,000 hours and divided by employee and contractor numbers. Due to an increase in RIDDOR Reportable, Lost time/Restricted work and Medical Treatment injuries in 2022/23 we did not achieve our target. However as part of our safety improvement plan we will be focusing on SGN safety and working towards 'zero harm' in SGN.
	Safe days	210	169	194	We fell short by 41 days, mainly due to lower class Road Traffic Collisions (RTCs) and cable damages. To focus on RTCs, fleet Opti-drive data that identifies good/poor drivers has been circulated to the business on a weekly basis, this can be examined locally and we are looking at coaching for our drivers around speeding/harsh breaking. A working group are now holding regular meetings focusing on reviewing performance and producing blogs/articles. To focus on the increased cable damages, we are establishing another working group, the initial action is to review the role of cable champions.
	Utilisation rate of employee assistance programme	8-12%	8%	10%	There has been a change in how utilisation rate is monitored, from clicks to logins on the platform. Therefore suggesting a drop in engagement. We offer a wide range of resources to our employees to support their health and wellbeing. Our Employee Assistance Programme is a fruitful resource for signposting, regarding health matters, financial issues, and mental health support such as counselling. This also includes 24/7 access to a virtual GP service offering prescriptions and advice.

Environment, Social and Governance (ESG) report

Prosperity

Aspect	Non-financial KPI	Target/ tracking	2022/23	2021/22	Comment
Creating a sustainable future for our business while providing a safe, reliable and affordable service	Economic contribution	Financial review, pages 32 to 38.			
	Financial investment contribution	Financial review, pages 32 to 38.			
	Total R&D expenses	Tracking	£2.6m	£2.1m	This shows the investment in ongoing innovation activities that are primarily supporting decarbonisation and/or protecting the environment. We are pleased that the number of projects having a positive impact on environment has almost doubled from five to nine in FY 2022/23. Projects such as stent bag (see page 22) reflect our commitment to tackling pressing environmental challenges and driving sustainable initiatives.
Maintaining an attractive and flourishing business respected by a wide range of stakeholders	New employee hires	Tracking	771 total new hires, 20% identified as female, 80% identified as male, 93% white, 7% ethnic minorities, 0% undisclosed, 72% aged between 21-40, 20% aged 40-60, 7% were aged 21, 1% were over 60	Of a total 297 new hires, we had the following gender and ethnicity split: 22% identified as female, 78% identified as male, 89% white, 10% ethnic minorities, 1% undisclosed, 72% aged between 21-40, 22% aged 40-60, 5% were aged under 21, 1% were over 60	Recruitment of the required number of operational, front-line employees has been made a Company-wide priority.
	Employee turnover	Tracking	11%	13%	
	Total tax paid	Financial review, pages 32 to 38.			

Looking ahead

It is our belief that publicly available disclosures have the opportunity to provide positive impact on our reputation. It gives our stakeholders including customers, new and existing talent, our Regulator and shareholders, lenders and rating agencies among others, information to evidence that SGN has responsibility at its core and is a positive contributor to a just energy transition. However, these metrics and frameworks alone do not provide a strategy and a vision for what SGN wants to achieve in ESG and Sustainability. We are therefore in the process of developing a new and coherent ESG and Sustainability strategy, with actionable outcomes. This strategy will consider how SGN impacts the climate, environment and society, as well as how these factors impact on our business.

Chair’s introduction to governance

On behalf of the Board, I am pleased to introduce our Corporate Governance report for 2022/23.

This report sets out how we satisfy the high standards of governance that are required of a regulated gas company, and are expected by our shareholders, regulators and wider stakeholders.

Board composition

The sale of their shareholdings by SSE, ADIA and OMERS, which completed at the start of the financial year, brought two new investors into the Company namely Canadian global asset manager Brookfield, taking on a 37.5% share and US based Global Infrastructure Partners, a leading global, independent infrastructure fund manager, now with a 25% share. As part of these transactions, Ontario Teachers’ Pension Plan, our third original investor, increased its ownership from 25% to 37.5% supported in its role by StepStone C Strategic Core Infrastructure Partnership.

Following the share sale, the Directors from SSE, ADIA and OMERS stepped down from the Board and we were pleased to welcome the incoming Directors nominated by the new shareholders: Michael Botha, Becky Lumlock, Jeff Rosenthal, Felipe Ortiz, Martin Catchpole, Paul Trimmer, Christian Fingerle and Michael Smart. Details of all Directors along with the alternate Directors can be found on pages 64 to 67 from which it can be seen we have a Board with a broad range of relevant experience and expertise.

Independent Directors

During the year the Board reviewed the requirements for the two sufficiently independent directors (SIDs) on the boards of Scotland Gas Networks plc (ScGN) and Southern Gas Networks plc (SoGN) and specifically the independence criteria set out in Standard Special Condition A42 and provision 10 of the Corporate Governance Code 2018 (together setting out the ‘Independence Criteria’). The Board considered the independence of the SIDs during the year. As part of its assessment, the Board considered the Independence Criteria. In particular, the Board noted the fact that Paul Jeffery and Laura Sandys had both served on the Board of ScGN and SoGN for over eight and four years respectively. The Board assessed, among other things, each of the above-named Director’s individual approach and contribution to Board discussions. It was concluded that each Director demonstrated ongoing objectivity which included appropriate challenges of matters under deliberation. Accordingly, the Board was of the opinion that the respective tenure did not interfere with the relevant Director’s ability to act in the best interests of ScGN and SoGN and are therefore considered each of them continued to be independent.

Board effectiveness review

As a Board, we remain committed to high standards of corporate governance and believe that these high standards are central to the effective management of the SGN Group and to maintaining the confidence of our stakeholders. We plan to undertake a full Board and committee performance effective review during 2023/24 and act on findings to ensure the highest standards of corporate governance.

Looking forward

I am grateful to the Board and all our employees for their commitment to creating value for all stakeholders and contributing to the good governance and stewardship of our business. During the coming year, the Board will continue to focus on safety, the Company’s recovery from our operational challenges, and the strategic opportunities presented by RIIO-GD3 and the Future of Energy.

Wates Corporate Governance Principles

SGN, under the Companies (Miscellaneous Reporting) Regulations 2018, has applied the Wates Corporate Governance Principles for Large Private Companies. This report sets out how the Wates Principles were applied.

For the year ended 31 March 2023, under the Companies (Miscellaneous Reporting) Regulations 2018, the SGN Group has applied the Wates Corporate Governance Principles for Large Private Companies, published by the Financial Reporting Council (FRC) in December 2018. A full copy can be viewed on its website under www.frc.org.uk/directors/corporate-governance-and-stewardship/governance-of-large-private-companies.

The Wates Principles provide a framework for the SGN Board to monitor corporate governance of the SGN Group and see where governance standards can be raised to a higher level across the business. We believe this, in turn, will result in better engagement with our stakeholder base.

The governance framework will also provide the right environment for the Board to make decisions for the long-term success of the SGN Group.

The tables on pages 57 to 59 summarise the six Wates Principles and indicate where more information can be found in the strategic and the governance reports. Throughout FY 2023/24, the Board will continue to review and challenge how the SGN Group can continue to improve its corporate governance.

Corporate governance requirements

The Board has considered the Companies (Miscellaneous Reporting) Regulations 2018 (the 'Regulations'). For accounting years beginning on or after 1 January 2019, companies which meet certain thresholds are required to report under four corporate governance reporting regimes:

1. **Employee Engagement** – A statement on how Directors have engaged with employees and how Directors have had regard to employee interests (see page 25 and Directors' Report on page 62).
2. **Stakeholder Engagement** – A statement on how Directors have engaged with stakeholders and how Directors have had regard to stakeholder interests (see pages 24 to 31 and Directors' Report on page 62).
3. **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 (see page 28).
4. **Corporate Governance** – A statement on the Company's Corporate Governance Arrangements and how these have been applied (see pages 56 to 60).

The SGN Group has adopted all four of these reporting regimes (Corporate Governance Requirements). In readiness, the Company has established a governance programme to ensure Directors both at Group Board and subsidiary Board level are able to comply with these Corporate Governance Requirements.

SGN and the Wates Principles for large privately owned companies

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.

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.

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.

Summary

Our purpose is to serve our communities by keeping everyone safe and warm. It's why we exist. Our values are safety, innovation, reliability, openness and respect. Our vision is to give our customers the best clean energy experience.

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

What we did in FY 2022/23 and what we plan to do in FY 2023/24

During the financial year, SGN's employees, the Executive Committee and the Board were engaged to establish the refreshed purpose, vision and values as represented above. More than 1,300 colleagues were involved in this engagement programme.

Looking ahead we will be developing our strategy out to 2030 to underpin our purpose, vision and stand as an organisation.

Where you can find further information

For further information on our purpose, vision and values please refer to pages 6 and 8.

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.

Summary

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 Group are effectively maintained. The Chief Executive, Chief Financial Officer and Company Secretary attend each Board meeting. Two Independent Non-Executive Directors also sit on the subsidiary Boards of Scotland and Southern Gas Networks plc.

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 Group 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.

What we did in FY 2022/23 and what we plan to do in FY 2023/24

At the start of the financial year, SGN's newly appointed six Directors undertook a comprehensive induction programme. These Directors bring a wealth of experience and come from a range of backgrounds.

The Board continues to remain committed to improving diversity throughout the Company in terms of gender, ethnicity, disability and age. This matter falls within the remit of the Board however its newly formed Board sub-committee, the Nomination Committee, actively engages with the shareholders to ensure that diversity remains a key objective for the selection and appointment of Directors.

The Board also re-appointed the two Independent Non-Executive Directors for an additional term, following consideration and satisfaction that they continued to meet the criteria set out in Gas Transporter Licence Standard Special Condition A42 and provision 10 of the Corporate Governance Code by demonstrating ongoing objectivity and continuing to provide valuable contribution based on their extensive experience and backgrounds.

In 2023/24 we propose to complete a Board skills audit to understand any gaps that we may need to close.

Where you can find further information

Further details of the Board composition and experience can be found on pages 64 to 67.

Wates Corporate Governance Principles

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.

Summary

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 in 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.

What we did in FY 2022/23 and what we plan to do in FY 2023/24

The Board continues to be supported by the work of the Board Committees. The Board Reserved Matters continues to be rolled out, 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.

In FY 2023/24, a Board effectiveness review will be undertaken now that the new Board has become fully embedded. A review of the Board training schedule is also planned to ensure the training provided to the Board remains robust and relevant for each year and will also be aligned with any training needs identified following the outcome of the Board effectiveness review.

Where you can find further information

Full details of how Directors fulfil their roles and discharge their responsibilities are found on pages 63 to 67.

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.

Summary

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 ensures 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 and Resilience Committee and financial risks by the Audit Committee.

What we did in FY 2022/23 and what we plan to do in FY 2023/24

The Board formally reviewed and challenged key principal risks and received bi-monthly updates on those with a high residual risk rating. The Board also reviewed key investment opportunities.

Our key principal risks are to be fully reassessed and associated risk appetite considered in the first half of 2023/24 with the Board.

Where you can find further information

The Group's risk management framework and key strategic risks and mitigations are outlined in the Strategic Report on pages 39 to 40. Details of the key investment opportunities reviewed by the Board can be found on page 68.

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.

Summary

The newly formed Remuneration Committee (previously the People & Reward Committee) has clearly defined terms of reference and is responsible for making recommendations to the Board concerning the Group'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 Group's resources by securing and retaining quality people who can deliver our purpose, vision and values and long-term goals for its existing and future stakeholders.

What we did in FY 2022/23 and what we plan to do in FY 2023/24

In FY 2022/23, the Board (following a recommendation from the Remuneration Committee) approved annual salary reviews of all personal service contract employees and agreed both the short-term and long-term incentive plan frameworks for the financial year and the three-year period starting April 2023 ensuring these frameworks measured both financial and non-financial performance.

In 2023/24 we plan to review the performance and reward structure of the Executive and wider group to ensure it reflects the strategy out to 2030.

Where you can find further information

Details of activities undertaken by the Remuneration Committee can be found on page 71. Details regarding the SGN Gender Pay Gap report information can be found on page 52.

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.

Summary

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 Group. The Board is committed to social responsibility, community engagement and environmental sustainability as underpinned by our strategic priorities.

What we did in FY 2022/23 and what we plan to do in FY 2023/24

Our Stakeholder, Environment, Social & Governance Committee (SESG) continued to meet during the year, taking account of stakeholder feedback and insight as they continued in their commitments to decarbonise the gas network and further develop our ESG strategy and reporting framework.

We will continue to build our engagement by agreeing a formal, but dynamic, Board stakeholder engagement plan to ensure we continue to foster relationships and put stakeholders at the heart of how we deliver our business.

Where you can find further information

Further details on Engaging with Stakeholders section and Section 172 (1) statement can be found on pages 24 to 31.

SGN governance structure

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

Governance framework

The successful execution of this strategy and oversight of its delivery are supported by clear Board protocols and a governance framework that defines relevant decision making authorities and responsibilities. Formally, these authorities and responsibilities are documented within: SGN's Articles of Association; Shareholder Agreement; the schedule of Matters Reserved for the Board; the terms of reference for the Committees; and the financial approval framework.

Chair

Our Board is led by our Chair, Nick Salmon, who was appointed on 1 March 2021 and is responsible for the effective running and management of the Board.

The roles of Chair and Chief Executive Officer are separate, with clear divisions of responsibilities.

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 Group and for setting 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 Group 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.

Board constitution and appointments

The Board of Directors comprises eight Non-Executive Directors. This consists of a Non-Executive Chair and seven Non-Executive Directors. The Board of Directors is the same for the Company and each subsidiary company within the Group, except for:

- Scotland Gas Networks plc and Southern Gas Networks plc, which consist of two additional independent Non-Executive Directors; and
- Subsidiary companies of SGN Place Limited, SGN Futures Limited, SGN Lessona Limited and SGN Gas to Grid ProjectCo1, which have their own Board of Directors.

Each of the Non-Executive Directors are chosen for their diversity of skills and experience.

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

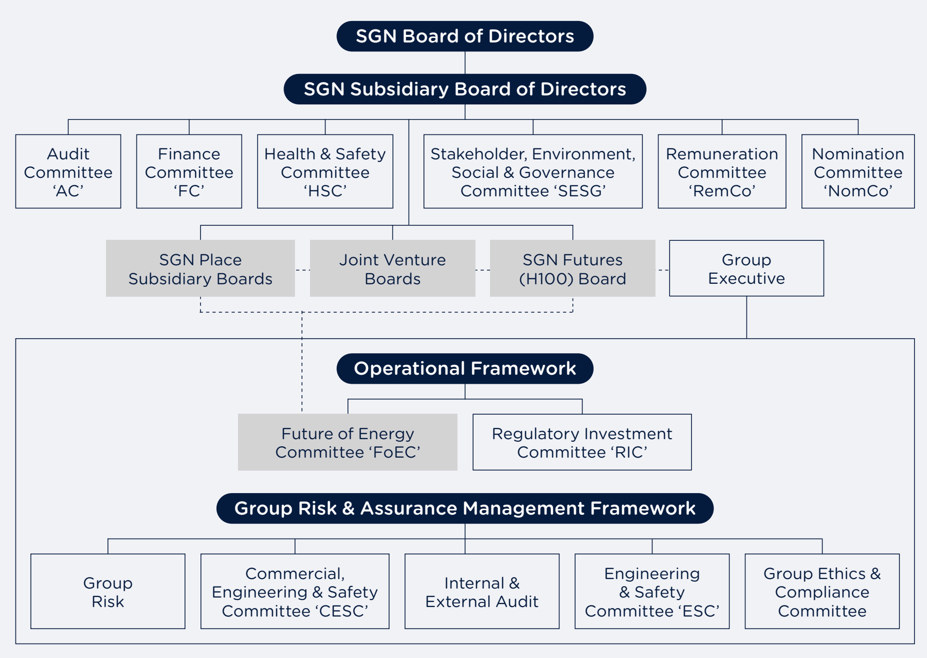
Roles and responsibilities for each Board Member, Chief Executive Officer, Chief Financial Officer and Group Company Secretary can be found on page 63 followed by their biographies on pages 64 to 67.

Board Committees

During the year the Board was directly assisted in the discharge of its duties by six Board Committees, 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 Committees hierarchy



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.

Further information on the Board committees are set on pages 69 to 74.

Board effectiveness

At the start of the financial year and as part of the share sale, SGN welcomed its newly appointed Board Directors. Within the first six-month period, the Chair, Interim Company Secretary and Chief Executive Officer took the opportunity to obtain the Board's initial feedback on Board and Committee effectiveness, including areas such as Board paper quality, timeliness, Board meetings and engagement. As the Board Directors are now fully embedded in their roles and SGN, we will undertake a full Board and Committee performance effective review and act on findings to ensure the highest standards of corporate governance.

Board and Executive reporting cycle

Chief Executive Officer and Chief Financial Officer

Below the Board, Executive responsibility rests with Mark Wild, 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 an Executive Management Team.

Biographical details for the CEO and CFO are set out on page 67.

Executive Committee

In FY 2022/23 the decision was made to split the Executive Committee into two forums, the Operational Executive Committee, and the Strategic Executive Committee. This was to ensure that the appropriate level of focus was given to Operational Performance and Strategic Planning respectively. The day-to-day management of the Company is delegated to these Committees which meet monthly and is chaired by the Chief Executive Officer and whose membership includes the Chief Financial Officer and leaders of each business unit. Both Committees are in turn supported by their 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. The Group Company Secretary has commenced work with Board Intelligence Limited to look at refreshing the Board and Committee paper templates, and the CEO report. As part of this, refresher training to paper authors on best practice paper writing to support the provision of high-quality information and effective decision making will be arranged. This exercise will involve reinforcing the use of best practice paper templates which seek to help focus the Board on what matters (including checks against its Section 172 duties). During the year, the Company dashboard (displaying key performance data and rapid insights on the overall health of the Group) was reviewed and redeveloped to streamline reporting across the Group. Board information continues to be 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. Biographical details for the Group Company Secretary are set out on page 67.

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 three supportive shareholders. The Board interacts with the shareholder members on a regular basis and always acts fairly with members of the Company.

Board meetings

There were six scheduled meetings of the Board and an additional two Board calls in 2022/23 in line with the agreed plan of business for the year, and details of Director attendance can be found on page 62.

In the months between full Board meetings, a Board update call provides the opportunity to discuss

SGN governance structure

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 six Board meetings and six Board update 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

The Board also ensures it spends time out of the Boardroom with stakeholders. During the year the Board undertook site visits and employee engagement sessions with a number of employees. The Board plans to resume stakeholder engagement sessions going forward. Full details of Board engagement with stakeholders can be found on pages 28 to 31.

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 (see page 63). 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 Group 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 Group, strategy related issues are discussed at every Board meeting.

The Board has also spent a significant time considering its strategy over the next five years with dedicated strategy sessions.

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 and Committee agendas during 2022/23 are set out on the following pages.

Meeting attendance, April 2022 to March 2023

	Board meetings	Audit Committee meetings	Finance Committee meetings	Health & Safety Committee meetings	Remuneration Committee meetings	Stakeholder, Environment, Social & Governance Committee meetings	Nomination Committee meetings**
Directors							
Charlotte Brunning	6/6	–	6/6	–	4/4	3/3	2/2
Michael Botha	6/6	3/3	6/6	–	–	–	2/2
Martin Catchpole	6/6	3/3	6/6	–	–	–	0/2
Christian Fingerle	6/6	–	–	–	–	–	2/2
Paul Jeffery	6/6	3/3	6/6	–	–	–	1/2
Rebecca Lumlock	6/6	–	–	3/3	4/4	3/3	2/2
Felipe Ortiz*	3/3	–	–	–	–	–	1/1
Jeff Rosenthal*	3/3	–	–	–	–	–	0/1
Nicholas Salmon	6/6	3/3	–	3/3	2/2	3/3	2/2
Laura Sandys	6/6	–	–	3/3	3/4	–	2/2
Paul Trimmer	6/6	–	–	3/3	4/4	3/3	2/2

* Jeff Rosenthal was appointed as a Director and Felipe Ortiz was appointed as an Alternate Director on 24 November 2022.
** Please find details regarding the membership of the Nomination Committee on page 74.

SGN Board roles and responsibilities

The below role specifications set out the clear division of responsibility between members of the Board and ensure adequate focus on areas central to its role.

Position	Responsible for
Chair	• Leading the effective operation and governance of the Board. • Setting agendas which support efficient and balanced decision-making. • Ensuring effective Board relationships and a culture that supports constructive discussion, challenge and debate. • Ensuring Board members are aware of and understand the views of key stakeholders. • Creating the conditions for overall Board effectiveness.
Chief Executive Officer	• Proposing and directing the delivery of strategy as agreed by the Board. • Leadership and day-to-day management of the Group and Executive Committee. • Engaging with SGN's six key stakeholder groups and leading on related activity. • Leading on unregulated activities.
Chief Financial Officer	• The financial performance of the Group and supporting the Chief Executive Officer in implementing strategy. • Proposing policy and actions to support sound financial management. • Overseeing relationships with debt investors.
Non-Executive Shareholder Directors	• Providing constructive challenge to the Board's decision-making processes. • Scrutinising, measuring and reviewing the performance of the Group. • Constructively challenging and assisting in the development of strategy. • Reviewing and challenging the performance of the Group's business against stakeholder interest.
Independent Non-Executive Directors	• Same responsibilities as Non-Executive Shareholder Directors, with the addition of: – Bringing independence to the Board and its decision-making process. – Providing independent insight and support based on relevant experience. – Assessing risk and the integrity of the financial information and controls. – Providing independent input into the Group's strategy to reflect stakeholder interests.
Company Secretary	• Compliance with Board procedures and supporting the Chair. • Ensuring the Board has high quality information, adequate time and the appropriate resources. • Advising and keeping the Board updated on corporate governance developments. • Considering Board effectiveness in conjunction with the Chair. • Facilitating the Directors' induction programmes and training. • Providing advice, services and support to all Directors as and when required.

Board of Directors

as at 31 March 2022

Chair

Nick Salmon

Board and Committee membership: Board; Audit Committee; Health & Safety Committee

Date of appointment: 14 March 2019

Biography: Nick joined the Board in March 2019 and was appointed the Chair of SGN in March 2021. He is also the Chair of Pressure Technologies plc. Previously he was Chair to South East Water Ltd, 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.

Key external appointments and changes during the period: Chair of Pressure Technologies Ltd

Shareholder Non-Executive Directors

Charlotte Brunning

Board and Committee membership: Board; Remuneration Committee; Finance Committee; Stakeholder, Environment, Social & Governance Committee

Date of appointment: 2 May 2018

Biography: 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, ADNOC, SGI and SGN Smart. Charlotte holds a BSc from the London School of Economics and an MBA from the London Business School.

Key external appointments and changes during the period: Director Apple Newco Limited; Director of Galaxy Pipeline Assets HoldCo Limited; Director of SGI; Director of Scottish Hydro Electric Transmission plc

Christian Fingerle

Board and Committee membership: Board

Date of appointment: 27 May 2022

Biography: Christian joined the Board in May 2022 and is a Senior Managing Director with the StepStone Group. Previously, he was a Member of the Management Board and Chief Investment Officer for Infrastructure at Allianz Capital Partners, responsible for a significant direct and indirect infrastructure investment programme and where he also held various board roles in portfolio companies. Prior to this, Christian worked in various roles within the Allianz Group and Technische Universität München.

Martin Catchpole

Board and Committee membership: Board; Audit Committee; Finance Committee

Date of appointment: 23 March 2022

Biography: Martin joined the Board in March 2022 and is a Principal at Global Infrastructure Partners (GIP) focusing on its energy and utility infrastructure investments across EMEA. Previously, he spent 16 years at Credit Suisse where he most recently was Co-Head of the Energy Group and Investment Banking. Martin is also a Chartered Accountant, qualifying with EY prior to his career in investment banking.

Key external appointments and changes during the period: Director of Galaxy Pipeline Assets HoldCo Limited

Shareholder Non-Executive Directors (cont)

Paul Trimmer

Board and Committee membership: Board; Remuneration Committee; Health & Safety Committee; Stakeholder, Environment, Social & Governance Committee

Date of appointment: 23 March 2022

Biography: Paul joined the Board in March 2022 and is a Senior Advisor to Global Infrastructure Partners (GIP) focusing on its energy sector. He has been a Board Director of FluxSwiss, CLH-PS and Interconnector UK and is an Advisory Board Member for Carbon Connect (an entity supporting the UK's transition to Net Zero). Previously, Paul spent 32 years at Shell, including as an Executive Director of Comgas and Transredes.

Key external appointments and changes during the period: Member of the Advisory Board of Carbon Connect; Partner in Atosú

Rebecca Lumlock

Board and Committee membership: Board; Remuneration Committee; Health & Safety Committee; Stakeholder, Environment, Social & Governance Committee

Date of appointment: 22 March 2022

Biography: Becky joined the Board in March 2022 and is an Operating Partner in Brookfield. She is also currently Interim CEO of Freightliner, the UK rail freight company. Prior to this she worked for Network Rail for five years including as the Managing Director for the Wessex Route, including London Waterloo. She was also their Group executive sponsor for gender. Becky has worked in the oil and gas industry for over 20 years across four continents, most recently as Managing Director of Dragon LNG, importing liquefied natural gas from around the world to help satisfy the UK's gas demand.

Key external appointments and changes during the period: Director of UK Gas Distribution 2 Limited; Director of Galaxy Pipeline Assets Holdco Limited; Director of PD Ports Limited

Jeff Rosenthal

Board and Committee membership: Board

Date of appointment: 24 November 2022

Biography: Jeff Rosenthal is a Managing Director and Operating Partner in Brookfield's Infrastructure Group. He also provides risk management, capital expenditure and ESG oversight as the Group's Chief Risk Officer.

Michael Botha

Board and Committee membership: Board; Audit Committee; Finance Committee

Date of appointment: 22 March 2022

Biography: Michael joined the Board in March 2022 and is an Operating Partner in Brookfield's Infrastructure Group overseeing operations, risk management and asset management activities. He has held senior positions across the organisation, including the Chief Risk Officer in Brookfield's Infrastructure Group, COO and CFO of Brookfield's private infrastructure funds business. Prior to joining Brookfield, Michael worked in the audit practice of a Big Four accounting firm.

Key external appointments and changes during the period:

Board of Directors

as at 31 March 2022

Statutory Independent Non-Executive Directors

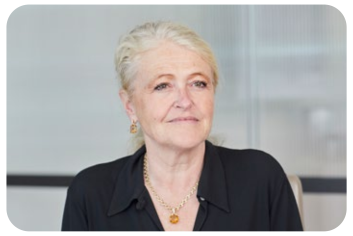
Paul Jeffery

Board and Committee membership
Board; Audit Committee; Finance Committee

Date of appointment
28 January 2014

Biography
Paul joined the Board in January 2014. Previously he ran the European Power, Utility and Infrastructure Investment Banking Sector team for Barclays. Paul is also a non-executive Director for UK Power Networks.

Key external appointments and changes during the period
Non-executive director of London Power Networks Ltd; Non-executive Director of South-Eastern Power Networks Ltd; Non-executive Director of Eastern Power Networks Ltd; Non-executive Director of UK Power Networks (IDNO) Ltd (all forming part of the UK Power Networks group)



Laura Sandys

Board and Committee membership
Board; Remuneration Committee; Health & Safety Committee; Stakeholder, Environment, Social & Governance Committee

Date of appointment
1 October 2018

Biography
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 the role of women 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.

Key external appointments and changes during the period
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 Highview Power; Director of Scottish Hydro Electric Transmission plc

Alternate Directors

Charles Thomazi

Date of appointment
26 October 2017

Biography
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.

Key external appointments and changes during the period
Director of Ontario Teachers' Pension Plan (OTPP); Director of Apple NewCo Limited; Director of Galaxy Pipelines Asset TopCo Limited; Sauna HoldCo Limited and related entities; Western TopCo Limited; Director of Scottish Hydro Electric Transmission plc

Michael Smart

Date of appointment
27 May 2022

Biography
Michael is a member of the infrastructure and real assets team at StepStone. Prior to joining StepStone, Michael was a Director in KPMG's Infrastructure Advisory Group, where he led the Energy Transition Strategy team. Michael was previously at National Grid in a variety of roles across operations, strategy, investor relations and M&A.

Felipe Ortiz

Date of appointment
24 November 2022

Biography
Felipe joined the Board in March 2022 and is a Managing Director in Brookfield's Infrastructure Group, responsible for leading the origination and execution of European deals for Brookfield's Super-Core Infrastructure fund. Since joining Brookfield in 2009, Felipe has led multiple infrastructure transactions that include global investments in the utilities, transportation and telecom sectors. Prior to joining Brookfield, he worked in an investment bank in New York, providing M&A and capital markets advisory to infrastructure funds.

Alternate Directors (cont)

Antoine Kerrenneur

Date of appointment
29 March 2023

Biography
Antoine joined the Board in March 2023 and is a Principal at Global Infrastructure Partners (GIP) focusing on its energy, renewables and utility infrastructure investments. Antoine joined GIP at its inception in 2006, prior to which he spent four years in the Investment Banking division of Credit Suisse in London.

Key external appointments and changes during the period
Director of the Board of Suez SA

Senior Management Team

Mark Wild OBE
Chief Executive Officer

Date of appointment
15 August 2022

Biography
Mark Wild joined SGN in August 2022 and has over 35 years of experience leading complex and critical infrastructure. Mark started his career in the electricity sector, but the majority of his experience has been in transportation, operating and building major infrastructure. Mark is the former Managing Director of Westinghouse Signals and was the CEO of Public Transport Victoria. Mark is the former Managing Director of London Underground and the former CEO of Crossrail, Europe's largest infrastructure programme.

Key external appointments and changes during the period
Independent Chair on the Transpennine Route Upgrade Board

Mick Carmedy
Chief Financial Officer

Date of appointment
22 January 2018

Biography
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 variety of financial, commercial and regulatory roles.

Nicola Graham-Shand
Chief of Staff and Director of Legal Services (Group Company Secretary)

Date of appointment
Company Secretary since July 2011

Biography
Nicola joined the Board as Company Secretary in July 2011. Nicola is the Chief of Staff and Director of Legal Services for SGN. Nicola 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.

Key external appointments and changes during the period
Non-Executive Director, FYLD Limited

Corporate information

Registered office
St Lawrence House
Station Approach
Horley, Surrey
RH6 9HJ

Auditor
Ernst & Young LLP
Statutory Auditor
London

Registered number
04958135

SGN Board activities during 2022/23

The SGN Board held six scheduled meetings and two further Board calls during the year ended 31 March 2023. The Board splits its time between steering and supervising the organisation across strategy, performance and governance in the short, medium and long term, which is discussed at each meeting of the Board. During the year the SGN Board focused on a number of areas as set out below.

Board focus

Strategy

- Supplier of Last Resort (SoLR), Third-Party Finance & Tariffs: consideration and approval of the SoLR and third-party finance strategy, and tariffs.
- Regulatory: consideration and approval of the Company's response to the Utility Regulator's (Northern Ireland) draft determination and received outcomes of the GD23 final determination.
- Customers: received and provided feedback on progress against the customer strategy and RIIO-GD2 customer experience programme to ensure RIIO-GD2 business plan requirements are met and maintain positive customer experience.
- Cyber Security & IT Resilience: continued to review IT resilience across the business and approved the ransomware policy.
- Energy Futures: reviewed the Energy Futures strategy covering the strategic framework, non-regulated activities, delivery of the strategy and future developments.
- ESG Reporting Framework: received an overview of ESG disclosures forming part of the World Economic Forum's Stakeholder Capitalism Metrics adopted by the Company's as the ESG reporting framework.
- Non-regulated growth: consideration and approval of new projects, investments and sales in property (SGN Place), MUA, (Yorkshire Water) gas to grid projects and opportunities which complement the core (Fleet, IT and Resourcing suppliers).

Performance

- Financial: review of long-term financial outlook and performance including consideration of dividend proposals, sufficient resources and approval of annual budget.
- Safety performance: the Board engaged significantly in monitoring, providing support and feedback with the development of the Safety Programme and performance initiatives, this included a dedicated additional safety deep dive session and continued Board site visits.
- Stakeholder: continued Board focus and review of stakeholder performance and initiatives, including receiving and reviewing the annual Customer, Stakeholder & Engagement Group report.
- Operations & Network: Deeper review of Southern and Scotland Operations and Network performance and initiatives. The Board also continue to closely monitor and discuss operational performance during the regular updates received against the Operations programme during the CEO Board update calls and Board meetings.
- Large projects and investments: review of progress against significant projects and investments, including H100 Fife and SGN Lessona Limited (Murphy Utility Assets).
- Employees: Received and provided feedback on SGN's Great Place to Work survey and continued focus on engagement with employees through 'let's chat' sessions and site visits. The Board regularly receive and closely monitor performance updates provided against the Resourcing Plan during the CEO Board update calls and Board meetings.
- Regulatory: continued Board focus and review of regulatory performance (including standards of service), initiatives and GD3 planning.

Governance

- Strategic risks – consideration of strategic risks (further details on pages 39 and 40) and implementing appropriate governance, monitoring compliance and ongoing risk management.
- Contract strategy and approvals – various significant contracts, including strategies, considered pursuant to the Board schedule of reserved matters.
- Policies and certificates – approved various Group policies and compliance certificates in line with the Governance Framework, such as the insurance renewal, modern slavery statement, sanctions policy and code of conduct.
- Governance – review and approval of the changes to the Board committee's membership (following the onboarding of new Directors), terms of references and formation of the Nomination Committee.

SGN Board Committees

Audit Committee

"The Committee continues to support the Group through an independent and robust review of financial and regulatory reporting and assurance processes."

Paul Jeffery
Audit Committee Chair

Appointment July 2020

Membership

The current members of the Audit Committee are **Paul Jeffery** (Committee Chair), **Nick Salmon**, **Michael Botha** and **Martin Catchpole**.

Attendees

The External Auditors are invited to attend the Audit Committee along with the following members of Management:

- Chief Financial Officer
- Head of Internal Audit, Risk and Compliance
- Finance Director
- Head of Financial Reporting and Tax

The role of the Committee and principal 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 and 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.
- Reviewed the accounting treatment and provisions for key commercial projects.
- Received and discussed the key outcomes from the Financial Reporting Council's review of the Annual Report and Accounts for the year ending 31 March 2022.
- Received and discussed the outputs from the property impairment review as required under Financial Reporting Standard 102.

External audit

- 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 external quality assessment undertaken on the Internal Audit function.
- 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 Group.
- 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 for Scotland Gas Network plc and Southern Gas Networks plc.
- Approved the financial compliance certificates for the MidCo Group.
- Monitored the level of non-audit fees and approved any new non-audit services.
- Reviewed the Data Assurance Guidelines for SGN.
- Reviewed the Prompt Payment Code return for SGN.

Looking forward

The Committee's priorities for FY 2023/24 are continuing to develop and improve our internal controls and assurance processes, with input from our internal and external auditors. The Committee will also monitor any proposed changes to the accounting standards adopted by the Group, to assess the impact and ensure compliance.

SGN Board Committees

Finance Committee

"The Committee maintained a financial risk management strategy that supports SGN's strong financial position and compliance with regulatory requirements during a period of evolving market conditions."

Michael Botha
Finance Committee Chair

Appointment November 2022

Membership

The current members of the Finance Committee are **Michael Botha** (Committee Chair), **Paul Jeffery**, **Martin Catchpole** and **Charlotte Brunning**.

Attendees

The following members of Management attend the Finance Committee:

- Chief Financial Officer
- Group Treasurer
- Finance Director

The role of the Committee and principal 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;
- policies for the operation of bank accounts and facilities, including appointment of authorised personnel to those accounts and facilities; and
- policies for 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 Finance Committee has been delegated authority by the Board to do so.

What the Committee has done this year

The Finance Committee held six meetings during the financial year of which three were additional to the planned. The Chair reports on key matters discussed to the Board and, where required, recommends 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 programme base prospectus and associated transaction documents.
- Considered and approved new financing and risk management strategies for the Group's near-term refinancing requirements.
- Reviewed and approved a strategy to manage the mandatory break in one of Scotland's interest rate swaps.
- Approved the commissioning of a capital restructure analysis.

Governance

- Reviewed and supported Management's proposal with regards to the Public Benefit Infrastructure Election.
- Reviewed and approved an update to the Treasury manual and bank and Treasury mandates.
- Received and discussed the Treasury audit findings.

Looking forward

The Committee's priorities for FY 2023/24 are to monitor the implementation of funding and financial risk management strategies approved in FY 2022/23 to ensure the Group has appropriate management of financial risk and that credit ratings are maintained within target levels. The Committee will also be focused on the refinancing of upcoming funding maturities within the Group to ensure that these are managed to maintain an appropriate funding profile and liquidity position.

Remuneration Committee

"We are delighted to be joined by Mark Wild, our new SGN CEO, and make other key Executive appointments in 2022/23 as we navigate a challenging recruitment and retention environment."

Charlotte Brunning
Remuneration Committee Chair

Appointment March 2022

Membership

The current members of the Remuneration Committee are **Charlotte Brunning** (Committee Chair), **Rebecca Lumlock**, **Paul Trimmer** and **Laura Sandys**.

Attendees

The following members of Management attend the Remuneration Committee:

- Chief Executive Officer
- HR & Services Director
- Head of Employee Relations, Policy & Reward

The role of the Committee and principal responsibilities

The Remuneration Committee is a sub-committee of the Board. The Remuneration 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 Executive performance, having regard to statutory and regulatory requirements;
- talent and succession strategy for the Group's Executive is suitable for the Group's long-term success;
- diversity and inclusion plays a key role across the Group; and
- employee feedback is listened to and acted on.

What the Committee has done this year

The Remuneration 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 development of the Company's resourcing plans designed to reinforce future resilience. These include the recruitment of significant numbers of front-line operational employees (including trainees and apprentices).
- Approved the annual salary review of all employees for cost-of-living increases.

Performance

- Reviewed and agreed short-term incentive plan (STIP) targets for the Financial Year, and long-term incentive plan (LTIP) targets for the three-year period ending 2025, ensuring both included a balanced scorecard of financial and non-financial performance.
- Approved the performance assessments for STIP for the prior Financial Year, and for LTIP for the 3-year period ending 31 March 2022.
- Reviewed and approved personal objectives for the Chief Executive Officer and Chief Financial Officer and assessed prior year performance.
- Reviewed the succession plan for Executive Directors and other critical roles.
- Reviewed the results of the 2022 'Great Place survey' (engagement), and action plans.

Governance

- Reviewed latest internal reward benchmarking results for Executive, senior and critical employees.
- Reviewed the Diversity & Inclusion Strategy.
- Monitored the recruitment process and appointment of the new CEO (Mark Wild) and the new Future of Energy Director.

Looking forward

The Committee's priorities for FY 2023/24 are to ensure the success of the Group's resourcing plans designed to reinforce future resilience, that the talent and succession strategy for the Group's Executive is suitable for the Group's long-term success and ensure diversity and inclusion continues to play a key role across the Group. The Committee will also review the reward strategy for the Group's Executive and senior/critical employees to ensure appropriate levels of incentivisation.

SGN Board Committees

Health & Safety Committee

"We are focusing on safety culture as we seek to move our safety performance from good to great."

Nick Salmon
Health & Safety Committee Chair

Appointment March 2022

Membership

The current members of the Health & Safety Committee are **Nick Salmon** (Committee Chair), **Laura Sandys**, **Rebecca Lumlock** and **Paul Trimmer**.

Attendees

The following members of Management attend the Health & Safety Committee:

- Chief Executive Officer
- Network & Safety Director
- Group Head of Safety & Environment

The role of the Committee and principal responsibilities

The Health & Safety Committee (HSC) is a sub-committee of the Board, and acts as a scrutineer to ensure the processes for managing health and safety risks are robust. This is delivered through four principles for effective leadership in health and safety: Plan, Do, Check and Act.

- Plan – Set the direction through approving effective health and safety policies; and set health and safety targets across a range of metrics covering members of public, staff and operational activities.
- Do – Monitoring the execution of those policy statements; reviewing and challenging performance against targets; and reviewing the compliance and assurance plan, and monitoring progress against key safety programmes.
- Check – Receive a comprehensive health and safety report for HSC committee; safety performance review and key updates in the CEO report and significant incident notifications from the CEO.
- Act – Receive an annual review of health and safety at the HSC; conduct Board member and Executive team site safety visits; and update on external audit reports to provide HSC assurance.

What the Committee has done this year

The Health & Safety 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

- Reviewed the project to update and transform the safety management framework.
- Received and discussed the Safety Programme.

Performance

- Reviewed and approved the Health and Safety targets across a range of metrics.
- Monitored and challenged performance and progress against the Health and Safety targets and scrutinised delivery plans.
- Reviewed the Fatigue programme performance.
- Reviewed compliance and assurance plans, including external assurance activity.
- Reviewed the Group's winter readiness and road traffic improvement plan.
- Received and discussed the safety benchmarking data compiled by the ENA across GDNs.
- Reviewed HSE interactions and investigations, including the Galpins Road incident.

Governance

- Reviewed and approved the Safety, Health and Environment Policy statement for FY 2022/23.

Looking forward

The Committee's priorities for FY 2023/24 are continuing to drive health and safety improvements ensuring that the Group achieves its commitment to getting everyone home safe and well. FY 2023/24 will see increasing focus on safety culture and a further drive in reporting and performance improvements for mental health and wellbeing. Also continued commitment across the Group for visible leadership through site engagements.

Stakeholder, Environment, Social & Governance Committee

"We are making good progress at the start of our ESG journey and have been harnessing the best knowledge to drive strong stakeholder and ESG outcomes throughout the business."

Laura Sandys
Stakeholder, Environment, Social & Governance Committee Chair

Appointment July 2022

Membership

The current members of the Stakeholder, Environment, Social & Governance Committee are **Laura Sandys** (Committee Chair), **Charlotte Brunning**, **Rebecca Lumlock** and **Paul Trimmer**.

Attendees

The following members of Management attend the Stakeholder, Environment, Social & Governance Committee:

- Chief Executive Officer
- Director of Stakeholder and Communications

The role of the Committee and principal responsibilities

The Stakeholder, Environment, Social & Governance Committee is a sub-committee of the Board. The Stakeholder, Environment, Social & Governance Committee's principal role is to support the Board in ensuring its Directors and the Company have due regard to:

- Cultural, environmental, social and governance (ESG) issues;
- all stakeholders with an interest or concern in the Company; 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, risks and emerging ESG issues.

What the Committee has done this year

The Stakeholder, Environment, Social & Governance 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

- Received and discussed the ESG disclosure metrics forming part of the ESG reporting framework.
- Received the Committee's planned activities for the calendar year and provided feedback.
- Received SGN's long-term community strategy and provided feedback.
- Received and discussed the Company's Community Support Programme for winter FY 2022/23.

Performance

- Reviewed performance against the RIIO-GD2 reporting requirements.
- Reviewed performance of the Company's stakeholder, environment and customer engagement activities and provided feedback.
- Received the Annual Environmental Report project update.
- Received a performance update against SGN's ESG and sustainability approach.
- Received an introduction to TCFD and SGN's approach to the disclosure requirements.

Governance

- Reviewed Directors' duties under S172 of the Companies Act 2006.
- Re-named the Committee to the Stakeholder, Environment, Social & Governance Committee.

Looking forward

The Committee's priorities for FY 2023/24 are to continue reviewing political engagement for the future of energy leading up to the UK Government's strategic decision on hydrogen in 2026 and to provide oversight of the support for fuel poor customers ensuring a just transition. The Committee will review the ESG & Sustainability vision and strategy including increased focus on interim and long-term greenhouse gas emissions target as well as opportunities and risks associated with climate change. The Committee will continue to oversee SGN's progress with ESG matters and will consider stakeholder engagement in preparation for business plan submission for the RIIO-GD3 price control.

SGN Board Committees

Nomination Committee

"We have established the Nomination Committee to formalise our processes for Board level appointments."

Nick Salmon
Nomination Committee Chair

Appointment November 2022

Membership

The current members of the Nomination Committee are **Nick Salmon** (Committee Chair), **Michael Botha** (as available), **Rebecca Lumlock** (as available), **Jeff Rosenthal** (as available), **Martin Catchpole** (as available), **Paul Trimmer** (as available), **Charlotte Brunning** (as available), **Christian Fingerle** (as available), **Paul Jeffery** (as available) and **Laura Sandys** (as available).

Attendees

The following members of Management attend the Nomination Committee:

- Chief Executive Officer
- HR & Services Director

The role of the Committee and principal responsibilities

The Nomination Committee is a sub-committee of the Board. The Nomination Committee's principal role is to support the Board by:

- Ensuring a formal, rigorous and transparent procedure is adhered to in the appointment of any new CEO/CFO or Independent Directors, to lead on the process for such appointments and make recommendations to the Board.
- Ensuring that the Board's composition is regularly reviewed and refreshed so that it is effective and able to operate in the best interests of its stakeholders.
- Reviewing and proposing the appropriate composition of Board committees and selection of Committee Chairs.

All decisions are recommended to the Board for approval.

What the Committee has done this year

The Nomination Committee held two 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:

Governance

- Formation of the Nomination Committee.
- Approved the appointment of the new Finance Committee Chair (Michael Botha).
- Approved the appointment of Jeff Rosenthal as Director and Felipe Ortiz and Antoine Kerrenneur as Alternate Directors to the SGN Group Boards.
- Approved the appointment of Sarah Peall, Jez Robinson, and Sharmila Sylvester to SGN Place subsidiary Boards. Review and approved the Environmental policy and targets for FY 2021.
- Reviewed the independence and approved the re-appointment of the Sufficiently Independent Directors for Southern Gas Networks PLC and Scotland Gas Networks PLC as required under Standard Special Condition A42 of the Gas Transporters Licence and provision 10 of the Corporate Governance Code 2018.
- Reviewed and agreed changes to the Committee terms of reference.

Looking forward

The Nomination Committee's priorities for FY 2023/24 are to ensure that any changes in appointment to the Board are successfully transitioned to ensure the right balance of skills and expertise as well as diversity.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent financial statements for each financial year. Under that law they are required to prepare the Group and parent Company 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 Group and parent Company and of their profit or loss for that period. In preparing each of the Group and parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable 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 Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent 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 parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent 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 Group and to prevent and detect fraud and other irregularities.

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

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

The Directors consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's and Company's position and performance, business model and strategy. Each of the Directors, whose names and functions are listed on pages 64 to 67 confirm that, to the best of their knowledge:

- the Group and Company Financial Statements, which have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006, give a true and fair view of the assets, liabilities, financial position and profit of the Group and profit of the Company; and
- the Directors' report contained in the Annual Report and Accounts includes a fair review of the development and performance of the business and the position of the Group and Company, together with a description of the principal risks and uncertainties that it faces.
- so far as the Director is aware, there is no relevant audit information of which the Group's and Company's auditors are unaware; and they have taken all the steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Group's and Company's auditors are aware of that information.

Signed on behalf of the Board of Directors of Scotia Gas Networks Limited:

Nick Salmon
Chair

27 July 2023

Overview
Strategic Report
Governance
Financial Statements

The Directors present their report and the audited consolidated financial statements for the year ended 31 March 2023.

The financial statements consolidate the financial statements of the Company and its subsidiary undertakings (together the 'Group'). This report must be read in conjunction with the Strategic Report found on pages 8 to 54.

Principal activities

The Company is a holding company which does not trade. The subsidiary undertakings principally affecting the profits or net assets of the Group in the year are listed in note 1 to the financial statements. The Group's principal activity is the development, administration, maintenance and safe operation of the Gas Distribution Networks in Scotland, southern England and Northern Ireland and the supply of associated transportation, connection and metering services. It will continue these activities for the foreseeable future.

Directors

The Directors of the Company who served during the year ended 31 March 2023 and up to the date of signing can be found on pages 64 to 67.

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, the Company 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.

Principal risks

The review of business for the year, including an analysis using key performance indicators and an indication of likely future developments in the business, together with a description of the principal risks and uncertainties facing the Group are set out in the Strategic Report on pages 39 to 40.

Employee engagement

The Group places 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 Group. 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.

Stakeholder engagement

Details of how the Directors have engaged with stakeholders can be found in the section 172 (1) statement on pages 24 to 31.

Corporate Responsibility

Corporate Responsibility continues to remain an integral part of the Group's business. The Group's approach, priorities and objectives in the corporate responsibility arena, specific to the environment and communities in which we work, are published, communicated and embedded within the business as part of the Group's overarching Strategic Pillars and ESG reporting. Further detail is set out in the Strategic Report on pages 45 to 54.

Research and Development

The Group is dedicated to innovation of methods and techniques, focusing on areas such as enhanced safety delivery, the development and integration of new materials and working techniques, energy efficiency and information modelling. Further detail on innovation is set out in the Strategic Report on pages 20 to 23.

Political contributions

The Group made no political contributions in the current or previous financial year.

Results and dividends

The consolidated profit and loss account is set out on page 85. The Group paid dividends of £54.5m in November 2022. No further dividends were declared.

Financial risk management

The Group's funding, liquidity and exposure to interest rates, foreign exchange and credit risks are managed within a framework of policies and guidelines which are authorised by the Board of Directors. Further detail on financial risk management is set out in the Strategic Report on pages 35 to 38.

Interest rate risk and inflation rate risk

The Group has interest bearing liabilities and as a matter of policy, a minimum of 75% of debt, excluding shareholder loans, is maintained at either fixed or inflation-linked rates of interest. The Group uses interest rate swaps and inflation-linked swaps, where necessary, in order to achieve the desired profile.

Liquidity risk

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

Foreign exchange risk

As a matter of policy, all debt denominated in a currency other than Pound Sterling must be fully hedged back to Pound Sterling at issuance.

Credit risk

The Company transacts with banks for the provision of interest rate and inflation rate hedging transactions. The Company takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy. 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.

Pricing risk

The Group's gas transportation charges are subject to price control formulae set within the regulatory regime. The Group'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, 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.

Going concern

The Group's financial position, cash flows, liquidity position and borrowing facilities together with the factors likely to affect its future performance and the Group's principal risks and uncertainties are set out in the Strategic Report on pages 39 to 40. The Group's financial risk management objectives and risk exposures are set out above.

As stated in the Strategic Report, the Group operates the regulated gas distribution networks in the south of England, Scotland and Northern Ireland. The revenue of the Group is regulated by Ofgem (for the south of England and Scotland) and UREGNI (for Northern Ireland) through established price control mechanisms based on the distribution network capacity. The Group has considerable financial resources together with committed financing facilities as discussed in note 18 of the financial statements, to finance the current and future operations.

The cost-of-living crisis and the conflict in Ukraine have impacted the global economy and, in light of this, the Group has performed additional analysis of its going concern of the Group as a whole, including performing scenario testing and sensitivity analysis.

These forecasts show the Group would be able to operate within its available committed liquidity (cash and bank facilities).

As a consequence, the Directors believe the Group is well placed to manage its business risks successfully. After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and for a period of at least 12 months following the approval of the Annual Report and Accounts (i.e. until 31 July 2024). Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Disclosure of information to auditors

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

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 they ought to have taken as a Director, to make themselves aware of any relevant audit information and to establish the Company's auditor is aware of that information.

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

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

By Order of the Board.

Nicola Graham-Shand
Company Secretary
27 July 2023

Report of the Independent Auditor

to the members of Scotia Gas Networks Limited

Opinion

In our opinion:

- Scotia Gas Networks Limited's Group financial statements and parent company financial statements (the 'financial statements') give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 March 2023 and of the Group's profit for the year then ended;
- the financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of Scotia Gas Networks Limited (the 'parent company') and its subsidiaries (the 'Group') for the year ended 31 March 2023 which comprise:

Group	Parent company
Consolidated balance sheet as at 31 March 2023	Balance sheet as at 31 March 2023
Consolidated profit and loss account for the year then ended	Statement of changes in equity for the year then ended
Consolidated statement of comprehensive income for the year then ended	Related notes 1 to 32 to the financial statements including a summary of significant accounting policies
Consolidated statement of changes in equity for the year then ended	
Consolidated cash flow statement for the year then ended	
Related notes 1 to 32 to the financial statements, 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).

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 Group and parent 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 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 Group and parent company's ability to continue to adopt the going concern basis of accounting included:

- 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 management's going concern model and performing mechanical integrity testing thereon, which is for the period to 31 July 2024, and which includes details of facilities available, covenant calculations, and the results of management's scenario planning;
- Comparing both the maturity profile of the debt and the covenants that are required to be met within the going concern period to the debt agreements;
- Challenging key assumptions within the forecasts with the assistance of our specialist teams and with reference to the RIIO-GD2 regulatory regime;
- Challenging management's forecasts with reference to the audited results for the year ended 31 March 2023;
- Evaluated how these forecasts have been revised to reflect any impact of climate change and the war in Ukraine;
- 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;
- 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 (including refinancing) 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 Group and parent company's ability to continue as a going concern for a period of 12 months (to 31 July 2024) from when the financial statements are authorised for issue.

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 Group and parent company's ability to continue as a going concern.

Overview of our audit approach

Audit scope	• We performed an audit of the complete financial information of 4 components and audit procedures on specific balances for a further 5 components. In addition, we performed specified audit procedures on specific balances for a further 12 components. • The components where we performed full, specific or specified audit procedures accounted for 100% of normalised and adjusted profit before tax, 100% of revenue and 100% of total assets.
Key audit matters	• Valuation of the defined benefit obligation.
Materiality	• Overall Group materiality of £6.6m which represents 5% of the Group's normalised and adjusted profit before tax. • The profit before tax is normalised and adjusted to exclude the accounting impacts of: – Incremental FY 2023 revenue due to exceptionally high wholesale gas prices in the prior year; and – A one off onerous contract provision accounted for in the year.

An overview of the scope of the parent company and Group audits

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each company within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of Group wide controls, changes in the business environment, the potential impact of climate change and other factors such as recent internal audit results when assessing the level of work to be performed at each company.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, of the 30 reporting components of the Group, we selected 21 components, which represent the principal business units within the Group. For these 21 components, all audit procedures were undertaken by the Group audit team. The remaining 9 components were holding companies, dormant companies or property companies which no longer hold any properties.

Of the 21 components selected, we performed an audit of the complete financial information of 4 components ('full scope components') which were selected based on their size or risk characteristics. For 5 components ('specific scope components'), we performed audit procedures on specific accounts within each component that we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile. For the remaining 12 components ('specified procedures components'), we performed audit procedures on specific accounts within those components in response to specific risk factors.

The reporting components where we performed audit procedures accounted for 100% (2022: 100%) of the Group's normalised and adjusted profit before tax, 100% (2022: 100%) of the Group's revenue and 100% (2022: 100%) of the Group's total assets.

Report of the Independent Auditor

to the members of Scotia Gas Networks Limited

For the current year, the full scope components contributed 96% (2022: 100%) of the Group's normalised and adjusted profit before tax, 98% (2022: 97%) of the Group's revenue and 98% (2022: 98%) of the Group's total assets.

The specific scope components contributed 3% (2022: 0%) of the Group's normalised and adjusted profit before tax, 2% (2022: 2%) of the Group's Revenue and 1% (2022: 1%) of the Group's Total assets.

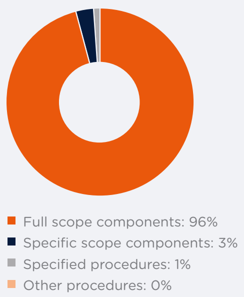
The audit scope of these components may not have included testing of all significant accounts of the component but will have contributed to the coverage of significant tested for the Group.

For 12 components we performed specified procedures over the valuation of inventory, the valuation of investments, the measurement of turnover, the existence of prepayments and accrued income, the completeness of accruals and the completeness and valuation of provisions.

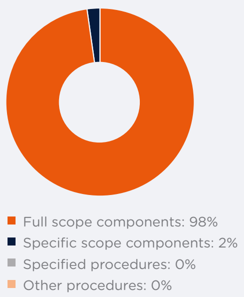
The remaining 9 components together represent 0% of the Group's normalised and adjusted profit before tax. For these components, we performed other procedures, including analytical reviews as well as testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the Group financial statements.

The charts below illustrate the coverage obtained from the work performed by our audit teams.

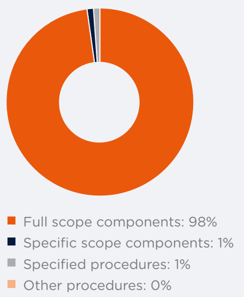
Normalised and adjusted profit before tax



Revenue



Total assets



Changes from the prior year

The number of selected components increased to 21 from 20 in the prior year due to increased activities in some components.

Climate change

Stakeholders are increasingly interested in how climate change will impact the Group. The Group has determined that the most significant future impacts from climate change on their operations will be from the impact of the shift towards a decarbonised energy system on the future of the gas network and managing changes as we move to a zero-carbon economy. These are explained on page 41 in the Task Force for Climate related Financial Disclosures. All of these disclosures form part of the 'Other information', rather than the audited financial statements. Our procedures on these unaudited disclosures therefore consisted solely of considering whether they are materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appear to be materially misstated, in line with our responsibilities on 'Other information'.

In planning and performing our audit we assessed the potential impacts of climate change on the Group's business and any consequential material impact on its financial statements.

The Group has explained in the 'key source of estimation uncertainty' section of the financial statements on page 99 how climate change has been reflected in the financial statements. The principal areas of consideration by management include the useful economic life of the gas networks and impairment of fixed assets.

Our audit effort in considering climate change was focused on evaluating management's assessment of the impact of climate risk and ensuring that the effects of material climate risks have been appropriately reflected by management in reaching their judgements in relation to the useful economic life of the networks and the impairment of fixed assets. We also challenged the Directors' considerations of climate change in their assessment of going concern and associated disclosures.

Based on our work we have not identified the impact of climate change on the financial statements to be a key audit matter or to impact a key audit matter.

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.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of the defined benefit obligation (£607.4m; Prior year comparative £858.7m) *Refer to the Audit Committee Report (page 10); Accounting policies (page 94); and Note 28 of the Consolidated Financial Statements (page 120)* The Group operates a defined benefit pension scheme. Significant estimates and judgements are made in valuing the Company's pension obligation. 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 Group's pension obligation. Key assumptions include pension salary increases, the mortality rate, the discount rate and the RPI and CPI inflation rates. 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 Group's financial position. The risk has increased in the current year due to market volatility impacting the key assumptions including interest rates and inflation.	We performed the following audit procedures at the 2 full scope components within which 100% of the defined benefit obligation balance is recorded: • 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, to determine whether the assumptions were within an appropriate range. This included pension salary increases, the mortality rate, the discount rate, and the 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; • Made inquiries of management and read the minutes of the meetings with Trustees, to confirm the completeness of accounting for any pension scheme transactions that have occurred in FY 2023; and • Assessed the compliance of the related disclosures under FRS 102.	Based on the audit procedures performed, we consider the valuation of the Group's defined benefit obligation for the year ended 31 March 2023 to be appropriate. The assumptions used in valuing the obligation were within acceptable EY ranges. We consider the disclosures to be appropriate and in accordance with FRS 102.

Report of the Independent Auditor

to the members of Scotia Gas Networks Limited

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.

We determined materiality for the Group to be £6.6m (2022: £8.8m), which is 5% (2022: 5%) of normalised and adjusted profit before tax so as to exclude the accounting impacts of incremental shrinkage revenues due to exceptionally high wholesale gas prices in the prior year and an onerous contract provision accounted for in the current year. We believe that normalised and adjusted 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.

We determined materiality for the Parent Company to be £17.7m (2022: £19.6m), which is 0.8% (2022: 0.9%) of total assets. However, since the Company was a full scope component, for accounts that were relevant for the Group financial statements, a performance materiality of £1.0m (2022: £1.3m) was applied.

Starting basis	• Profit before tax of £150.8m
Adjustments	• Remove shrinkage revenues of £30.8m • Add back onerous provision of £15.9m
Materiality	• Normalised and adjusted profit before tax of £135.9m • Materiality of £6.6m (5% of materiality basis)

During the course of our audit, we reassessed initial materiality and changed our materiality basis from FY 2023 forecast profit before tax to FY 2023 normalised and adjusted profit before tax. We changed our basis to exclude the impact of transactions which are caused by fluctuating market conditions and infrequent material transactions.

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 Group's overall control environment, our judgement was that performance materiality was 75% (2022: 75%) of our planning materiality, namely £4.9m (2022: £6.6m). We have set performance materiality at this percentage following a quantitative and qualitative assessment of prior year misstatements and our assessment of the Group's overall control environment.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £1.0m to £4.9m (2022: £1.3m to £5.9m).

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 £0.3m (2022: £0.4m), 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 set out on pages 1 to 77, other than the financial statements and our auditor's report thereon. The Directors are responsible for the other information contained within 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' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the 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 by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit

Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement set out on page 75, 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 Group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities 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.

Report of the Independent Auditor

to the members of Scotia Gas Networks Limited

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect 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 Group 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 Group operates in a regulated market; it is subject to regulations from the national regulatory authorities in Great Britain and Northern Ireland.
- We understood how the Group 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 Group'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 Group 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 testing journal entries that met our defined risk criteria based on our understanding of the business, testing a sample of journals which include a manual posting to revenue, 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, Group 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.

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.

Steven Dobson (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

27 July 2023

Consolidated profit and loss account

for the year ended 31 March 2023

	Notes	2023 £m	2022 £m
Turnover (i)	3, 4	**1,288.5**	1,115.9
Net operating costs (ii)	4	**(849.0)**	(751.6)
Operating profit	4	**439.5**	364.3
Interest receivable and similar income	8	**23.1**	8.8
Interest payable and similar expenses	9	**(310.6)**	(226.4)
Fair value movements on derivatives	6	**(1.1)**	(74.2)
Share of loss of investments in JV entities	15	**(0.1)**	(1.4)
Profit before tax	5	**150.8**	71.1
Tax	10	**(55.6)**	(258.3)
Profit/(loss) for the year	25	**95.2**	(187.2)

(i) Included within turnover are exceptional items to the sum of £30.8m (2022: £nil), see note 6 for further details.
(ii) Included within operating costs are exceptional items to the sum of £15.9m (2021: £30.8m), see note 6 for more details.

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

The accompanying notes form part of these financial statements.

Consolidated statement of comprehensive income

for the year ended 31 March 2023

	Notes	2023 £m	2022 £m
Profit/(loss) for the financial year	25	**95.2**	(187.2)
Cash flow hedges:			
– Profit arising on cash flow hedges	25	**21.0**	15.5
Remeasurement on net pension asset	28	**(117.1)**	57.1
Deferred tax movement relating to components of other comprehensive income:			
– Cash flow hedges	25	**(5.3)**	0.6
– Pension asset		**29.3**	(19.6)
Other comprehensive (loss)/income for the year		**(72.1)**	53.6
Total comprehensive income/(loss)		**23.1**	(133.6)

The accompanying notes form part of these financial statements.

Balance sheets

as at 31 March 2023

	Notes	Group 2023 £m	Group 2022 £m	Company 2023 £m	Company 2022 £m
Fixed assets					
Intangible assets	13	**333.7**	347.5	**–**	–
Tangible assets	14	**7,225.4**	7,022.5	**–**	–
Investments	15	**11.9**	10.5	**2,030.7**	2,030.7
Non-current financial assets	18	**4.8**	–	**–**	–
		7,575.8	7,380.5	**2,030.7**	2,030.7
Current assets					
Inventories	16	**43.5**	49.6	**–**	–
Debtors	17	**205.8**	167.1	**62.6**	80.5
Short term deposits		**245.9**	95.5	**–**	–
Cash at bank and in hand		**43.3**	27.1	**–**	0.9
		538.5	339.3	**62.6**	81.4
Creditors: amounts falling due within one year	19	**(668.6)**	(602.8)	**(11.3)**	(10.4)
Net current (liabilities)/assets		**(130.1)**	(263.5)	**51.3**	71.0
Total assets less current liabilities		**7,445.7**	7,117.0	**2,082.0**	2,101.7
Creditors: amounts falling due after more than one year	20	**(5,211.6)**	(5,015.0)	**(356.3)**	(356.3)
Provisions for liabilities	22	**(1,138.9)**	(1,111.6)	**(0.1)**	–
Deferred income	23	**(490.9)**	(471.2)	**–**	–
Net assets excluding pension asset		**604.3**	519.2	**1,725.6**	1,745.4
Defined benefit pension asset	28	**246.0**	362.5	**–**	–
Net assets including pension asset		**850.3**	881.7	**1,725.6**	1,745.4
Capital and reserves					
Called up share capital	24	**200.0**	200.0	**200.0**	200.0
Hedging reserve		**(25.2)**	(40.9)	**–**	–
Profit and loss account		**675.5**	722.6	**1,525.6**	1,545.4
Shareholders' funds	25	**850.3**	881.7	**1,725.6**	1,745.4

The accompanying notes form part of these financial statements.

The Company has elected to take the exemption under Section 408 of the Companies Act 2006 from presenting the parent company profit and loss account. The Company's profit for the year amounted to £34.7m (2022: £78.8m).

The financial statements of Scotia Gas Networks Limited, registered number 04958135, were approved by the Board of Directors and authorised for issue on 27 July 2023.

Signed on behalf of the Board of Directors

Nick Salmon
Chair

Consolidated statement of changes in equity

for the year ended 31 March 2023

	Notes	Called up share capital £m	Hedge reserve £m	Profit and loss account £m	**Total £m**
Group:					
At 1 April 2021		200.0	(57.0)	956.3	**1,099.3**
(Loss) for the financial year		–	–	(187.2)	**(187.2)**
Cash flow hedges		–	15.5	–	**15.5**
Remeasurement of net defined benefit pension asset		–	–	57.1	**57.1**
Deferred tax movements relating to items of other comprehensive income:					
– Cash flow hedges		–	0.6	–	**0.6**
– Pension asset		–	–	(19.6)	**(19.6)**
Total comprehensive (loss)		–	16.1	(149.7)	**(133.6)**
Transactions with owners, recognised directly in equity					
Dividends paid	12	–	–	(84.0)	**(84.0)**
At 31 March 2022		200.0	(40.9)	722.6	**881.7**
Profit for the financial year		–	–	95.2	**95.2**
Cash flow hedges	25	–	21.0	–	**21.0**
Remeasurement of net defined benefit pension asset	28	–	–	(117.1)	**(117.1)**
Deferred tax movements relating to items of other comprehensive income:	25				
– Cash flow hedges		–	(5.3)	–	**(5.3)**
– Pension asset		–	–	29.3	**29.3**
Total comprehensive income		–	15.7	7.4	**23.1**
Transactions with owners, recognised directly in equity					
Dividends paid	12	–	–	(54.5)	**(54.5)**
At 31 March 2023		200.0	(25.2)	675.5	**850.3**

The accompanying notes form part of these financial statements.

Company statement of changes in equity

for the year ended 31 March 2023

	Notes	Called up share capital £m	Profit and loss account £m	**Total £m**
Company:				
At 1 April 2021		200.0	1,550.6	**1,750.6**
Profit for the financial year	11	–	78.8	**78.8**
Total comprehensive income		–	78.8	**78.8**
Transactions with owners, recognised directly in equity				
Dividends paid	12	–	(84.0)	**(84.0)**
At 31 March 2022		200.0	1,545.4	**1,745.4**
Profit for the financial year	11	–	34.7	**34.7**
Total comprehensive income		–	34.7	**34.7**
Transactions with owners, recognised directly in equity				
Dividends paid	12	–	(54.5)	**(54.5)**
At 31 March 2023		200.0	1,525.6	**1,725.6**

The accompanying notes form part of these financial statements.

Consolidated cash flow statement

for the year ended 31 March 2023

	Notes	2023 £m	2022 £m
Cash flows from operating activities			
Operating profit	4	439.5	364.3
Depreciation and software amortisation	13, 14	201.3	195.5
Goodwill amortisation	13	9.5	9.6
Amortisation of deferred income	23	(11.7)	(10.7)
Loss on disposal of fixed assets		4.7	4.7
Decrease/(increase) in inventories	16	2.8	(4.7)
(Increase)/decrease in debtors	17	(25.2)	9.6
Increase/(decrease) in creditors and employee benefits	19, 20	60.6	(9.8)
Increase in provisions	22	27.2	1.5
Other operating cash flows		0.4	–
Cash generated by operations		709.1	560.0
Interest paid		(157.2)	(144.8)
Tax paid		(41.6)	(38.2)
Net cash inflow from operating activities		510.3	377.0
Cash flows from investing activities			
Interest received		2.2	0.3
Purchase of fixed assets		(396.3)	(342.0)
Purchase of intangible fixed assets		(8.7)	(7.8)
Sale of tangible fixed assets		3.2	0.7
Customer contributions received		33.0	37.0
Fixed asset investment additions		(1.4)	(5.0)
Net cash outflow from investing activities		(368.0)	(316.8)
Cash flows from financing activities			
Shareholder loan interest paid		(30.6)	(30.7)
Issue of debt		399.0	30.0
Dividend paid	12	(54.5)	(84.0)
Repayment of debt		(308.7)	(122.1)
Payments of mirror swaps	31	-	(27.8)
Payments of interest rate swaps		(2.8)	(4.4)
Receipts from inflation-linked swaps		21.9	12.8
Net cash inflow/(outflow) from financing activities		24.3	(226.2)
Net increase/(decrease) in cash and cash equivalents		166.6	(166.0)
Cash and cash equivalents at beginning of the year		122.6	288.6
Cash and cash equivalents at the end of the year (i)		289.2	122.6

(i) Cash and cash equivalents of £289.2m includes £41.4m of cash which has specific restrictions over its use. See note 1 for further details.

The accompanying notes form part of these financial statements.

Notes to the financial statements

for the year ended 31 March 2023

1. Principal accounting policies

The financial statements have been prepared in accordance with applicable accounting standards in the United Kingdom and the Companies Act 2006.

The financial statements of the Group present the results for the year ended 31 March 2023. The comparative period presented is the year ended 31 March 2022.

A summary of the more significant Group accounting policies, which have been applied consistently in both years is as follows.

General information and basis of preparation
Scotia Gas Networks Limited 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 registered number is 04958135. The Company and its subsidiary undertakings together form the 'Group' for which consolidated financial statements are drawn up. The Group's principal activity is the development, administration, maintenance and operation of the Southern and Scotland gas distribution systems, the supply of gas transportation services and other gas related services.

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. Amounts are expressed in millions of pounds, except where noted otherwise.

The functional currency of Scotia Gas Networks Limited and its subsidiary undertakings is considered to be Pound Sterling because that is the currency of the primary economic environment in which the Company and its subsidiary undertakings operate. Amounts are expressed in millions of pounds, except where noted otherwise.

The parent company is included in the consolidated financial statements, and is considered to be a qualifying entity under FRS 102 paragraphs 1.8 to 1.12. The following exemptions available under FRS 102 in respect of certain disclosures for the parent company financial statements have been applied:

- The reconciliation of the number of shares outstanding from the beginning to the end of the period has not been included a second time;
- No separate parent company Cash Flow Statement with related notes is included; and
- Certain disclosures required by FRS 102.11 Basic Financial Instruments and FRS 102.12 Other Financial Instrument Issues in respect of financial instruments not falling within the fair value accounting rules of Paragraph 36(4) of Schedule 1.

Basis of consolidation
The financial statements consolidate the financial statements of the Company and its subsidiary undertakings drawn up to 31 March each year. Subsidiaries are those entities controlled by the Group or the Company.

Subsidiaries acquired are consolidated in the financial statements of the Group from the date that control commences until the date control ceases, using the acquisition method of accounting.

Intra-Group balances and any unrealised gains and losses or income and expenses arising from intra-Group transactions, are eliminated in preparing the consolidated financial statements.

Going concern
As at 31 March 2023 the financial statements have been prepared on a going concern basis which the Directors consider to be appropriate for the following reasons.

After reviewing the Group's forecasts and projections, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future and for a period of 12 months following the approval of the Annual Report and Accounts (i.e. until 31 July 2024). A significant proportion of the Group's revenue is fixed by the regulatory charging methodology improving the predictability of cash flows and mitigating risks. The base case scenario assumes that there will be no new debt issuance in the forecast period that has not been secured before the reporting date, but it includes £300m of debt due for repayment in October 2023. The base case scenario also considers high inflation, together with the expected impact this has on the Group's cash flows in the forecast period.

Notes to the financial statements

for the year ended 31 March 2023

1. Principal accounting policies (continued)

Considerations are made by the Directors for severe but plausible downside scenarios. These downside scenarios include, most notably, a decline in transportation revenue due to a decline in demand and an increase in operating costs as a result of inflation and supply chain pressures. In these downside scenarios, the business has sufficient headroom on its existing banking facilities to maintain sufficient liquidity in the short and long term, and to satisfy the lenders' covenants.

Additionally, management performed reverse stress testing to overstretch the Group's liquidity. This yielded scenarios which are considered highly remote due to the predictability of the Group's cash flows under the regulatory mechanism.

Consequently, the Directors are confident that the Company will have sufficient funds to continue to meet its liabilities as they fall due for the foreseeable future and for a period of 12 months following the approval of the Annual Report and Accounts (i.e. until 31 July 2024) and consequently have prepared the financial statements on a going concern basis.

The UK Government's commitment to reduce greenhouse gas emissions to net zero by 2050 has a profound impact on the future of our gas network. As outlined in the Chief Executive's report, the Group is taking considerable steps to ensure that our network can be repurposed to transport greener gases, for example hydrogen, thereby extending the life of our network to 2050 and beyond.

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 amortised on a straight line basis over its useful economic life, which is estimated to be 50 years. Impairment indicators for goodwill are assessed on an annual basis at each balance sheet date in line with FRS 102 requirements.

Intangible assets – software
Software assets are included at cost, net of depreciation and any provision for impairment. Amortisation is provided on a straight-line basis over a period of three to ten years, which is their estimated useful economic life. The Group's intangible assets have a remaining useful economic life ranging between one to five years.

Tangible fixed assets
Tangible fixed assets are stated at cost, net of depreciation and any provision for impairment. 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 provided on all tangible fixed assets, other than investment properties and freehold land, at rates calculated to write off 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.

In line with the relevant accounting standards replacement expenditure is capitalised and the useful life is based on the range within mains and services above. Tangible fixed assets are derecognised on disposal, or when no future economic benefits are expected from its use or disposal. Major components are treated as separate assets where they have significantly different patterns of consumption of economic benefits and are depreciated separately over their useful lives.

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.

Interest receivable and Interest payable
Interest payable and similar expenses include interest payable on borrowings 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.

Interest receivable and similar income includes 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.

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.

Other fixed asset investments are held at cost.

Investments in joint ventures
The Group's joint ventures are accounted for using the equity method of accounting where the joint venture investments are carried at historical cost plus the Group's share of post-acquisition results, less any impairment in value. The Group recognises its share of the results of these equity-accounted operations after tax and interest in the income statement.

Construction contracts
Turnover and cost of sales attributable to construction contracts is recognised using a percentage of completion method based on cost incurred to date plus profit, where profit can be reliably measured.

Inventories
Inventories are stated at the lower of cost and estimated selling price less costs to sell, which is equivalent to the net realisable value. Cost includes materials, direct labour and an attributable proportion of manufacturing overheads based on normal levels of activity. Cost is calculated using the FIFO (first-in, first-out) method. A provision is made for obsolete, slow-moving or defective items where appropriate.

Through the Group's property companies, there is land in the course of remediation, sale or development which is included within inventories. It is measured at the lower of cost (inclusive of the associated provision for the expected future cost to demolish any gas holders and remediate land to a statutory level) and net realisable value.

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.

Goodwill impairment
The recoverable amount of goodwill is the higher of the value in use or the fair value less cost to dispose. This 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. The Company considers there to be two separate cost generating units (CGUs) for the purpose of goodwill impairment: Southern Gas Networks plc and Scotland Gas Networks plc. Goodwill impairment is not reversed.

Other non-financial assets
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.

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

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

Notes to the financial statements

for the year ended 31 March 2023

1. Principal accounting policies (continued)

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 Group 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 Group 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 year in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

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.

Turnover also includes income from sales of surplus land through the Group's property companies. Turnover is recognised at the point of completion and is stated net of value added tax.

Turnover attributable to construction contracts is recognised using a percentage of completion method based on cost incurred to date plus profit, where profit can be reliably measured.

Employee benefits
Defined benefit pension scheme
The Group operates a Group-wide defined benefit pension plan. The Company is the entity legally responsible for the Group-wide defined benefit pension plan. The net defined benefit cost of the plan is charged to participating entities based on the proportionate number of members relating to each company. The contributions payable by the participating entities are determined on the same basis as the charging policy detailed 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 Group, 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 Group, 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 Group as an income tax.

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.

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.

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.

Grants and contributions
1) 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 profit and loss on a straight line basis over the estimated life of the related asset. The corresponding asset is capitalised within fixed assets and is depreciated over its useful economic life. Customer contributions which have been received by the end of the financial year, for which the corresponding asset has not yet been delivered, are treated as creditors due within one year.

2) Government grants
Government grants in respect of additions to fixed assets are treated as deferred income and released to turnover in the profit and loss account over the estimated life of the related assets.

Provisions
A provision is recognised in the balance sheet when the Group 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. Change in estimates are recognised in profit or loss unless they are related to inventory, in which case such changes are recognised in inventory. No provision is required for the repair of gas pipes as these are replaced on an agreed basis with the Regulator.

Onerous contracts
A contract is considered onerous, where the unavoidable costs of meeting the obligations under a contract exceed the economic benefits expected to be received under it. The unavoidable costs reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. The Group recognises a provision for the present obligation under the onerous contract. If the Group has assets that are dedicated to the contract, these are reviewed for impairment.

Contingent liabilities
Through the ordinary course of operations, the Company is party to various litigation, claims and investigations. Where management consider the settlement of these to be possible or the amount of the obligation cannot be estimated reliably, the Group treats this as a contingent liability until such a time that it becomes probable that the Group will be required to make a payment or the obligation can be estimated reliably.

Financial instruments
FRS 102 sections 11 and 12 give an accounting policy choice for financial instruments. The Group 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 Group 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 Group after deducting all of its liabilities.

The Group'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.

Notes to the financial statements

for the year ended 31 March 2023

1. Principal accounting policies (continued)

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).

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.

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.

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.

Derecognition of financial assets
The Group 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.

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 there is a difference between the asset's carrying amount and the present value of estimated cash flows, discounted at the asset's original effective interest rate. Subsequent recoveries of amounts previously written off are credited to the profit or loss.

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. The Group receives monies in the form of grants and contributions towards innovation projects. The use of this cash is restricted by the specific terms and conditions of each project.

Short term deposits
Short term deposits comprise of cash deposits that are available with notice of more than 24 hours (one day). These relate to money market funds with an original maturity date of three months or less.

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

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 Group 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 Group's documented risk management or investment strategy and information about the Group 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.

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.

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.

De-recognition of financial liabilities
The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Derivative financial instruments
The Group uses derivative financial instruments for risk management purposes.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

The best evidence of fair value is a quoted price for an identical asset in an active market. When quoted prices are unavailable, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the market is not active and recent transactions of an identical asset on their own are not a good estimate of fair value, the fair value is estimated by using a valuation technique.

Hedge accounting
Where the derivative is designated as a hedging instrument, on inception of the hedge relationship, the Group 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 Group 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.

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.

1. Principal accounting policies (continued)

Exceptional items
Management utilises an exceptional items framework that follows a three-step process which considers the nature of the event, the financial materiality involved and any particular facts and circumstances. In considering the nature of the event, management focuses on whether the event is within the Group's control and whether the event is considered to be one-off in nature. In determining the facts and circumstances, management considers factors such as ensuring consistent treatment between favourable and unfavourable transactions, precedent for similar items, number of periods over which costs will be spread or gains earned and the commercial context for the particular transaction.

Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets and inventories, significant changes in provisions, gains or losses on disposals of businesses or investments, or other one-off material events.

Fair value movements on derivatives
Fair value movements comprise gains or losses recorded in the income statement arising from the changes in fair value of derivative financial instruments to the extent that hedge accounting is not achieved or it is not effective.

New and amended standards and interpretations
Published in FRED 82 Draft amendments to FRS 102, the Financial Reporting Council proposes significant changes to the approach to revenue recognition and accounting for leases, alongside a number of other amendments. The proposed effective date for these amendments is accounting periods beginning on or after 1 January 2025 (i.e. the year ended 31 March 2026 for the Group). Management expects FRED 82 to have a material impact on the Group's revenue recognition for customer contributions as well as for leases.

2. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group'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 Group incur significant staff and contractor costs for fulfilling normal business activities. Management judgement is required to allocate costs between capital, replacement and operating expenditure depending on the nature of the work being performed. Capital and replacement expenditure as reported in the Strategic Report on page 32 are both recognised as additions to plant and equipment within tangible fixed assets. Operating expenditure is recognised within Net operating costs within the Profit and Loss account.

b. Impairment of fixed assets – As set out in note 1 above, management has exercised judgement during the Group balance sheet review when identifying impairment indicators impacting the goodwill on the CGUs.

c. Exceptional items – The categorisation of certain items as exceptional follows a three-step process which considers the nature of the event, materiality involved and any particular facts and circumstances. Management focuses on whether the event is within the Group's control and whether the event is considered to be one-off in nature. See note 6.

d. Supplier of last resort – Management has given consideration to the Supplier of Last Resort (SoLR) mechanism under the Group's regulatory transportation licences. The Group accounts for SoLR payments as levies, and as such will only be obliged to pay the costs when reciprocating incremental levies are received. In relation to the SoLR mechanism, the Group does not hold inventory risk, does not set the SoLR mechanism pricing and is not exposed to credit risk. As such, it is management's judgement that the Group is acting as an Agent and therefore associated revenues and costs are not shown within Turnover or Net operating costs within the Profit and Loss account. The SoLR mechanisms only impact on the current and prior year financial statements is an immaterial balance originating from timing differences in payment and recovery, which is recorded in other creditors on the Balance Sheet.

e. Customer contributions – Cash inflows are presented as cash flows from investing activities in the Consolidated cash flow statement, as customer contributions are directly associated with capital investment in the Group's gas networks.

f. Galpin's Road Investigation – Management judgement is required in assessing if the recognition criteria for a provision has been met in relation to the Galpin's Road incident as at 31 March 2023 (as described on page 2).

Based on external legal advice, management has concluded that the investigation is not sufficiently progressed to reliably estimate the financial impact or timing of any future obligation. As such the case has been disclosed as a contingent liability (see note 27) until the point at which any economic transfer can be reliably estimated.

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 note 28 and include: the discount rate on scheme liabilities, mortality rates, pension increases, salary increases and inflation. The Group 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 and demolition provision – In assessing the degree of contamination at the various sites estimation is required where elements of the contamination are underground. Additional uncertainty exists for the costs to demolish the gas holders. In these cases, it is difficult to assess with any certainty the extent of the contamination and demolition required. The discount rate is also a source of estimation. See note 22.

e. Climate change – In assessing the impact of climate change on the Group, management has considered two key areas being useful economic life and impairment of fixed assets. Management believes the role of hydrogen in the UK's energy transition will support both the UEL of the networks and the recoverable amount of the respective CGUs. Therefore the Group assesses there is currently limited exposure to climate related risks.

f. Onerous contract provision – the Group recognises an onerous provision in respect of the obligation to complete the H100 Fife project to construct an end-to-end hydrogen system for approximately 300 homes in Scotland. The provision represents management's best estimates of the future expenditure necessary to settle the obligations.

g. Operational target provision – During the year, the Group failed to meet the 97% target imposed by the Gas Transporter Standard Special Conditions D10 in relation to the time taken to respond to gas escapes in both Southern Gas Networks plc and Scotland Gas Networks plc. As at 31 March 2023 management considers the recognition criteria for a provision to have been met, as there is a probable future economic transfer resulting from the missed target.

Significant management estimation is required to assess the quantum of the provision. Management used historical cases from other Gas Distribution Networks as the basis of the provision estimate.

3. Turnover

The Board and Chief operating decision maker view the Group as one operating segment. Analysis of turnover by class of business:

	2023 £m	2022 £m
Transportation of natural gas and the provision of related services	**1,243.2**	1,055.4
Gas asset services	**18.9**	17.8
Gas to the West construction contract	**8.3**	7.0
Property sales	**15.4**	30.2
Managed service income	**2.0**	5.0
Other income	**0.7**	0.5
Total turnover	**1,288.5**	1,115.9

Gas to the West construction contract revenue is recognised with reference to stage of completion based on costs incurred as a proportion of total forecasted expenditure.

Other income relates to property rental income.

Turnover arises in the United Kingdom and is attributable to the continuing activity of transportation of natural gas and the provision of related services, which the Directors consider a single class of business.

Notes to the financial statements

for the year ended 31 March 2023

4. Operating profit and net operating costs

	2023 £m	2022 £m
Turnover	**1,288.5**	1,115.9
Cost of sales	**(54.4)**	(48.9)
Operational and administrative expenses	**(590.8)**	(503.6)
Depreciation	**(188.3)**	(182.8)
Amortisation	**(22.5)**	(22.3)
Loss on disposal of fixed assets	**(4.7)**	(4.7)
Other operating income	**11.7**	10.7
Total net operating costs	**(849.0)**	(751.6)
Operating profit	**439.5**	364.3

5. Profit before taxation

Group profit before taxation is stated after charging/(crediting):

	2023 £m	2022 £m
Auditor's remuneration	**0.7**	0.6
Amortisation of goodwill	**9.5**	9.6
Amortisation of intangible assets	**13.0**	12.7
Depreciation of tangible fixed assets	**188.3**	182.8
Amortisation of customer contributions	**(11.7)**	(10.7)
Loss on disposal of fixed assets	**4.7**	4.7
Rental under operating leases	**4.8**	8.9

Auditor's remuneration for the Group comprises:

- Audit of these financial statements £33,000 (2022: £22,320)
- Audit of financial statements of subsidiaries of the Company £562,000 (2022: £463,280)
- Audit-related assurance services £105,000 (2022: £99,200)
- Other assurance services £70,000 (2022: £37,200)

6. Exceptional items and fair value movements on derivatives

	2023 £m	2022 £m
Exceptional items included within turnover:		
Incremental turnover from recovery of costs due to increase in gas wholesale prices (i)	**(30.8)**	–
Exceptional items included within net operating costs:		
Cost impact of increase in gas wholesale prices (i)	**-**	30.8
Onerous contract (ii)	**15.9**	–
Included within taxation:		
Tax charge/(credit) on impact of increase in gas wholesale prices	**5.9**	(5.9)
Tax (credit) on onerous contract	**(1.6)**	–
Total tax charge/(credit) included within taxation	**4.3**	(5.9)
Fair value movements on derivatives:		
Net losses on derivative financial instruments (iii)	**1.1**	74.2
Included within taxation:		
Tax charge/(credit) on derivative financial instruments	**4.0**	(16.4)

(i) In the year, the Group recorded incremental turnover as a result of recovering incremental costs charged in the prior year of £30.8m (2022: nil) associated with the rise in wholesale gas prices through its regulated tariffs. These incremental costs were disclosed as exceptional items in the prior year and as such the associated income received in the current year is disclosed as such.
(ii) During the year, the Group recognised an onerous contract provision of £15.9m (2022: nil) in respect of the obligation to complete the H100 Fife project to construct an end-to-end hydrogen system for approximately 300 homes in Scotland.
(iii) Net losses on derivative financial instruments comprise gains and losses arising on derivative financial instruments reported in the Statement of Profit and Loss. These exclude gains and losses for which hedge accounting has been effective, which has been recognised directly in the statement of comprehensive income. Included within net losses on derivative financial instruments is £70.6m (2022: £35.6m) of accretion on CPI-linked swaps. There was nil impact (2022: £nil) to the cash flow as a result of the fair value movements on financial derivatives.

7. Employee information and Directors' emoluments

The Group had 4,068 full time equivalent employees as of 31 March 2023 (2022: 3,698). The average monthly number of full time equivalent employees during the year was 3,874 (2022: 3,710).

	2023	2022
Field based staff	**2,140**	1,958
Office and other administrative staff	**1,928**	1,741
Total	**4,068**	3,698

The Independent Directors received aggregate remuneration of £201,528 (2022: £198,648) for their services to the Group during the year. There are seven 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 Company's shareholders, do not specifically receive any remuneration in respect of the Company, and the time spent working as a Board member on SGN was deemed immaterial.

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

	2023 £m	2022 £m
Staff costs		
Wages and salaries	**192.5**	166.9
Social security costs	**22.7**	18.6
Pension costs (see note 28)	**35.8**	35.7
Total	**251.0**	221.2

The Company had four employees as of 31 March 2023 (2022: 5).

8. Interest receivable and similar income

	2023 £m	2022 £m
Net defined benefit pension income (see note 28)	**10.1**	6.0
Other interest receivable	**13.0**	2.8
Total	**23.1**	8.8

9. Interest payable and similar expenses

	2023 £m	2022 £m
Interest payable on fixed rate instruments	**120.8**	107.4
Interest payable on floating rate instruments	**6.7**	2.9
Interest payable on inflation-linked instruments	**130.9**	73.3
Shareholder loan	**30.6**	30.7
Other interest payable	**19.9**	11.0
Unwinding of discount	**1.7**	1.1
	310.6	226.4

Included within interest payable on inflation-linked instruments is £133.0m of accretion on RPI-linked debt instruments (2022: £57.9m).

Notes to the financial statements

for the year ended 31 March 2023

9. Interest payable and similar expenses (continued)

In March 2022, the Group agreed to settle outstanding fees due in relation to certain guarantees provided by Ambac Assurance UK Limited that were previously in place over certain outstanding public bond instruments, but which were removed in November 2020. The cash settlement amount of £4.3m is included within the interest paid line of the cash flow statement for the comparative period.

10. Tax charge on profit

a) Analysis of the tax charge on profit

	2023 £m	2022 £m
Current tax		
UK corporation tax on profits for the year	33.8	34.4
Adjustment in respect of previous years	(4.6)	0.1
Total current tax charge	29.2	34.5
Deferred tax		
Origination and reversal of timing differences	11.4	(13.0)
Adjustments in respect of previous years	7.0	(5.4)
Effect of change in tax rate	8.0	242.2
Total deferred tax charge	26.4	223.8
Total tax charge on profit	55.6	258.3

b) Factors affecting the total tax charge for the year

	2023 £m	2022 £m
Profit before tax	150.8	71.1
Profit multiplied by standard rate of corporation tax in the UK of 19% (2022: 19%)	28.7	13.5
Effects of:		
Expenses not deductible for tax purposes	4.8	0.5
Non deductible goodwill	1.8	1.8
Depreciation of non qualifying assets	0.9	0.9
De-recognition of deferred tax relating to previous years	4.6	1.4
Current year deferred tax not recognised	5.1	4.2
Adjustment in respect of prior years	2.4	(5.3)
Permanent benefit of capital allowances super deduction	(0.7)	(0.9)
Effect of change in tax rate	8.0	242.2
Total tax charge on profit	55.6	258.3

The standard rate of tax applied to reported profit on ordinary activities is 19% (2022: 19%). Finance Act 2021 increased the main rate of corporation tax from 19% to 25% from 1 April 2023. As these changes have been substantively enacted at the comparative period's balance sheet date, deferred tax has been calculated accordingly and this has had the effect of increasing the Group's deferred tax liability at 31 March 2023 by £8.0m (2022: £242.2m).

11. Profit of the Company for the financial year

The Company's profit for the year amounted to £34.7m (2022: £78.8m). The intercompany interest receivable during the year ended 31 March 2023 amounted to £2.1m (2022: £0.8m) in the Company. In accordance with the exemption available under section 408 of the Companies Act 2006, no separate profit and loss account is presented in respect of the Company.

12. Dividends

	2023 £m	2022 £m
Equity shares		
Interim dividends paid of 11.5945p (2022: 17.8704p)	54.5	84.0

The dividends paid in the current year of £54.5m were paid in November 2022.

13. Intangible fixed assets

	Goodwill £m	Software £m	Total £m
Group			
Cost			
At 1 April 2022	477.6	198.7	676.3
Additions	–	8.7	8.7
Disposals	–	(105.7)	(105.7)
At 31 March 2023	477.6	101.7	579.3
Amortisation			
At 1 April 2022	161.1	167.7	328.8
Charge for the year	9.5	13.0	22.5
Eliminated on disposal	–	(105.7)	(105.7)
At 31 March 2023	170.6	75.0	245.6
Net book value			
At 31 March 2023	307.0	26.7	333.7
At 31 March 2022	316.5	31.0	347.5

The goodwill, which arose on the acquisitions of Scotland Gas Networks plc and Southern Gas Networks plc, is being amortised on a straight-line basis over 50 years, with 32 years remaining. 50 years is the expected life of the network and is consistent with the long-term outlook of the Regulator.

Goodwill is monitored by management for two operating units as follows:

	2023 £m	2022 £m
Southern Gas Networks plc	210.0	216.5
Scotland Gas Networks plc	97.0	100.0
	307.0	316.5

The carrying value of goodwill was reviewed at the reporting date and assessed for any indicators of impairment. Where indicators of impairment are identified, a full impairment test of goodwill is required. As at 31 March 2023, following management's assessment of internal and external impairment indicators, no such indicators were noted. As such £nil impairment charge has been recorded for the current year (2022: £nil).

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

There is no security held against the intangible fixed assets.

During the year, the Group wrote off £105.7m of fully depreciated assets, with a nil net book value.

Notes to the financial statements

for the year ended 31 March 2023

14. Tangible fixed assets

Group	Short leasehold properties £m	Freehold properties £m	Plant and machinery £m	Motor vehicles and office equipment £m	Total £m
Cost					
At 1 April 2022	0.7	146.4	8,723.1	149.3	9,019.5
Additions	–	9.1	372.2	19.4	400.7
Disposals	–	–	(23.2)	(4.0)	(27.2)
Impairment	–	(0.7)	(1.3)	–	(2.0)
At 31 March 2023	**0.7**	**154.8**	**9,070.8**	**164.7**	**9,391.0**
Depreciation					
At 1 April 2022	0.3	51.4	1,844.2	101.1	1,997.0
Charge for the year	–	5.7	170.8	11.8	188.3
Disposals	–	–	(15.3)	(4.0)	(19.3)
Impairment	–	(0.1)	(0.3)	–	(0.4)
At 31 March 2023	**0.3**	**57.0**	**1,999.4**	**108.9**	**2,165.6**
Net book value					
At 31 March 2023	**0.4**	**97.8**	**7,071.4**	**55.8**	**7,225.4**
At 31 March 2022	0.4	95.0	6,878.9	48.2	7,022.5

There is no security held against the fixed assets. Included within freehold properties is the Net book value of land of £17.4m (2022: £17.4m).

The Company had no tangible fixed assets in either year.

15. Fixed asset investments

	Group		Company	
Cost	**2023 £m**	2022 £m	**2023 £m**	2022 £m
Shares in Group undertakings				
At 1 April	**–**	–	**2,028.4**	2,028.4
At 31 March	**–**	–	**2,028.4**	2,028.4
Investments in joint ventures				
At 1 April	**8.1**	5.5	**–**	–
Additions[1]	**1.5**	4.0	**–**	–
Share of losses in joint venture	**(0.1)**	(1.4)	**–**	–
At 31 March	**9.5**	8.1	**–**	–
Other investments[2]				
At 1 April	**2.4**	1.4	**2.3**	1.3
Additions	**–**	1.0	**–**	1.0
At 31 March	**2.4**	2.4	**2.3**	2.3
Total investments	**11.9**	10.5	**2,030.7**	2,030.7

(1) Additions relates to additional funding requirements in Murphy Asset Services Limited.
(2) Other investments are investments in companies over which the Group is not considered to have significant influence.

Subsidiary undertakings, joint ventures and other investments

The undertakings in which the Company's interest at the year-end is 20% or more as follows:

Name	Description of shares held	% of shareholding	Country of registration	Principal activities
Subsidiaries – directly held				
SGN PledgeCo Limited	2,517,000,001 ordinary shares of £0.01	100%	England & Wales	Holding company
SGN Place Limited	1 ordinary share of £1	100%	England & Wales	Holding company
SGN Connections Limited	1 ordinary share of £1	100%	England & Wales	Supply of gas connection services
SGN Commercial Services Limited	1 ordinary share of £1	100%	England & Wales	Meter asset manager and supply of commercial services
SGN Smart Limited	1 ordinary share of £1	100%	England & Wales	Supply of managed services
SGN Lessona Limited	1 ordinary share of £1	100%	England & Wales	Holding company
SGN Futures Limited	1 ordinary share of £1	100%	England & Wales	Holding company
SGN Heat Networks Limited	1 ordinary share of £1	100%	England & Wales	Holding company
Subsidiaries – indirectly held				
Southern Gas Networks plc	160,174,771 ordinary shares of £1	100%	England & Wales	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services
Scotland Gas Networks plc	49,392,787 ordinary shares of £1	100%	Scotland	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services
SGN Contracting Limited	1 ordinary share of £1	100%	England & Wales	Supply of contracting services
SGN Natural Gas Limited	1 ordinary share of £1	100%	England & Wales	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services
SGN Midco Limited	2,815,000,001 ordinary shares of £1	100%	England & Wales	Holding company
SGN Property Holdings Limited	18,022,565 ordinary shares of £1	100%	England & Wales	Property development
SGN Property Services Limited	340,856 ordinary shares of £1	100%	England & Wales	Property development
SGN Belvedere Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Brighton Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Southampton Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Epsom Limited	373,414 ordinary shares of £1	100%	England & Wales	Property development
SGN Greenwich Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Motspur Park Limited	1,539,420 ordinary shares of £1	100%	England & Wales	Property development
SGN Old Kent Road Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Rotherhithe Limited	1 ordinary share of £1	100%	England & Wales	Property development
Tonbridge Riverside Regeneration Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Rotherhithe Holdco Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Croydon Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Crayford Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Futures (H100) Limited	1 ordinary share of £1	100%	England & Wales	Property development
SGN Silvertown LLP	Equity	100%	England & Wales	Dormant

Notes to the financial statements

for the year ended 31 March 2023

15. Fixed asset investments (continued)

Name	Description of shares held	% of shareholding	Country of registration	Principal activities
Joint ventures				
Murphy Asset Services Limited	250 ordinary shares of £1	50%	England & Wales	Operation of utility distributions systems
SGN Mitheridge Limited	1 ordinary share of £1	50%	England & Wales	Property development
Other fixed asset investments				
XoServe Limited	23,020 ordinary shares of £0.01	23.02%	England & Wales	Provision of transportation services on behalf of all the major gas network transportation companies
FYLD Limited	13,262,643 ordinary shares of £0,0001	10%	England & Wales	Software development

The registered address of Scotland Gas networks plc is Axis House, 5 Loanhead Drive, Newbridge, Edinburgh, EH28 8TC. The registered address of all other subsidiaries above is St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ.

The address of Murphy Asset Services Limited's registered office is Hiview House, Highgate Road, London, NW5 1TN. The joint venture's financial year end is 31 December. The aggregate amount of capital and reserves of the undertaking as at 31 March 2023 was £11.4m (2022: £10.5m). Its loss for the year then ended was £2.1m (2022: £2.5m).

The address of SGN Mitheridge Limited's registered office is Langham Hall UK Services LLP, 8th Floor, 1 Fleet Place, London, EC4M 7RA. The aggregate amount of capital and reserves of the undertaking as at 31 March 2023 was £1.7m (2022: £4.5m deficit). Its profit for the year then ended was £7.2m (2022: £2.6m loss).

Other fixed asset investments are held at cost.

The address of the registered office of XoServe Limited is Lansdowne Gate, 65 New Road, Solihull, B91 BDL. The XoServe Limited operating results for the year ended 31 March 2023 are not considered material to the Group's financial statements.

16. Inventories

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Work in progress	**43.0**	49.1	**-**	–
Finished goods	**0.5**	0.5	**-**	–
	43.5	49.6	**-**	–

Included within work in progress is £42.8m (2022: £42.8m) of land.

The amount of inventory recognised as an expense in the year amounted to £6.9m (2022: £1.2m).

17. Debtors

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Trade debtors	**134.6**	119.8	**-**	–
Prepayments and accrued income	**48.8**	39.0	**-**	–
Deferred tax asset	**-**	–	**-**	6.0
Amounts owed by Group undertakings	**-**	–	**62.6**	74.5
Other debtors	**3.5**	2.3	**-**	–
Corporation tax	**18.9**	6.0	**-**	–
	205.8	167.1	**62.6**	80.5

Included in debtors are amounts falling due after more than one year of £9.8m (2022: £11.6m).

Included in prepayments and accrued income is accrued income on the Gas to the West project of £24.5m (2022: £16.8m).

Amounts owed by Group undertakings for the Company include intercompany loans due from SGN Commercial Services Limited amounting to £40.4m (2022: £57.2m); due from SGN Place Limited amounting to £6.9m (2022: £6.7m); and due from SGN Lessona Limited amounting to £13.1m (2022: £11.0m). The loans bear interest at the Bank of England Base Rate plus 1% per annum and are repayable on demand. Also included in the balance are intercompany trade balances due from the SGN Group subsidiaries of £2.2m (2022: £0.4m).

18. Non-current financial assets

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Derivative financial instruments – interest rate swaps not in hedge relationships	**4.8**	–	**-**	–

19. Creditors: amounts falling due within one year

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
£300m 4.875% fixed rate note due 2023(1)	**299.8**	–	**-**	–
Inflation-linked debt: £165m 2.127% RPI-linked note due 2022(1)	**-**	266.2	**-**	–
Floating-rate debt: bank facility	**-**	30.0	**-**	–
Trade creditors	**81.9**	51.2	**1.1**	0.1
Other taxation and social security	**23.6**	25.2	**-**	–
Other creditors	**18.4**	17.9	**-**	–
Accrued interest	**56.4**	51.5	**10.2**	10.3
Accruals	**134.7**	108.6	**-**	–
Deferred income	**53.8**	52.2	**-**	–
	668.6	602.8	**11.3**	10.4

(1) Listed on the London Stock Exchange.

The Group held three committed bank facilities at 31 March 2023:

- £20m (2022: £235m) revolving credit facility at Scotland Gas Networks plc maturing in March 2025, this facility was undrawn at 31 March 2023 (2022: undrawn);
- £340m (2022: £125m) revolving credit facility at Southern Gas Networks plc maturing in March 2025, this facility was undrawn at 31 March 2023 (2022: £30m drawn);
- £25m debt service reserve facility at SGN MidCo Ltd maturing in January 2024, this facility was undrawn at 31 March 2023 (2022: undrawn).

Notes to the financial statements

for the year ended 31 March 2023

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

	Group		Company	
Borrowings	**2023 £m**	2022 £m	**2023 £m**	2022 £m
Fixed rate debt				
£300m 4.875% fixed rate note due 2023[1]	**-**	299.6	**-**	–
£350m 2.5% fixed rate note due 2025[1]	**349.3**	348.9	**-**	–
£35m 2.407% fixed rate loan due 2025	**35.0**	35.0	**-**	–
£250m 3.25% fixed rate note due 2027[1]	**249.0**	248.7	**-**	–
£375m 4.875% fixed rate note due 2029[1]	**374.5**	374.4	**-**	–
£100m 2.9% fixed rate note due 2030	**99.1**	99.0	**-**	–
£75m 2.74% fixed rate note due 2030	**74.8**	74.8	**-**	–
£75m 2.74% fixed rate note due 2030	**74.8**	74.8	**-**	–
£250m 1.25% fixed rate note due 2031[1]	**248.3**	248.1	**-**	–
£75m 1.98% fixed rate note due 2032	**74.8**	74.8	**-**	–
£34m 6.220% fixed rate note due 2032	**33.8**	–	**-**	–
£50m 2.04% fixed rate note due 2033	**49.9**	49.8	**-**	–
£185m 3.02% fixed rate note due 2033	**183.0**	183.0	**-**	–
£75m 2.87% fixed rate note due 2033	**74.8**	74.8	**-**	–
£75m 2.87% fixed rate note due 2033	**74.8**	74.8	**-**	–
$66m 5.630% fixed rate note due 2033	**53.1**	–	**-**	–
£100m 2.27% fixed rate note due 2034	**99.6**	99.6	**-**	–
£225m 4.875% fixed rate note due 2034[1]	**224.7**	224.7	**-**	–
£30m 6.310% fixed rate note due 2035	**29.8**	–	**-**	–
£50m 6.220% fixed rate note due 2035	**49.8**	–	**-**	–
$66m 5.730% fixed rate note due 2035	**53.1**	–	**-**	–
£400m 3.1% fixed rate note due 2036[1]	**398.1**	397.9	**-**	–
£70m 6.340% fixed rate note due 2037	**69.8**	–	**-**	–
£15m 3.11% fixed rate note due 2038	**14.8**	14.8	**-**	–
£225m 6.375% fixed rate note due 2040[1]	**224.2**	224.2	**-**	–
	3,212.9	3,221.7		–
Inflation-linked debt				
£150m 2.066% RPI-linked note due 2025[1]	**272.9**	242.1	**-**	–
£83.3m 2.013% RPI-linked note due 2025[1]	**151.5**	134.4	**-**	–
£15m 2.580% RPI-linked loan due 2028	**24.5**	21.9	**-**	–
£50m -0.8818% CPI-linked note due 2029	**55.0**	–	**-**	–
£50m -0.4465% CPI-linked note due 2032	**55.0**	–	**-**	–
£37.5m 0.11% RPI-linked note due 2033	**48.7**	43.1	**-**	–
£83.3m 2.013% RPI-linked note due 2035[1]	**151.6**	134.4	**-**	–
£87.5m 0.28% RPI-linked note due 2038	**113.5**	100.5	**-**	–
£125m 2.317% RPI-linked note due 2039[1]	**209.6**	185.0	**-**	–
	1,082.3	861.4	**-**	–
Floating rate debt				
£125m floating rate loan due 2025	**125.0**	125.0	**-**	–
£80m floating rate loan due 2026	**80.0**	80.0	**-**	–
£60m floating rate loan due 2026	**60.0**	60.0	**-**	–
£30m floating rate loan due 2026	**30.0**	30.0	**-**	–
£35m floating rate loan due 2026	**35.0**	35.0	**-**	–
£35m floating rate loan due 2026	**35.0**	35.0	**-**	–
£80m floating rate note due 2043[1]	**79.7**	79.7	**-**	–
	444.7	444.7	**-**	–

	Group		Company	
Borrowings (cont)	**2023 £m**	2022 £m	**2023 £m**	2022 £m
Total external borrowings	**4,739.9**	4,527.8	**-**	–
Shareholders' loans[2] (see note 29)	**356.3**	356.3	**356.3**	356.3
Total borrowings	**5,096.2**	4,884.1	**356.3**	356.3
Derivative financial instruments				
Inflation-linked swaps (see note 21)	**73.0**	74.2	**-**	–
Interest rate swaps (see note 21)	**27.7**	56.7	**-**	–
Cross-currency swaps (see note 21)	**14.7**	–	**-**	–
Total creditors falling due after more than one year	**5,211.6**	5,015.0	**356.3**	356.3

The shareholder loans, which are subordinated, are redeemable at par on 9 April 2043 and carry a fixed interest rate of 8.6%. The Company may, upon giving due notice, elect to pay some or all of the interest payable through the issuance of further loans to shareholders.

(1) Listed on the London Stock Exchange.
(2) £178.2m of the shareholder loan is listed on The International Stock Exchange.

Maturity of borrowings

	Group	
	2023 £m	2022 £m
Due within one year	**299.8**	296.2
Between one and five years	**1,422.8**	1,673.3
After five years	**3,673.4**	3,210.8
	5,396.0	5,180.3

The Company's borrowings all fall due by 9 April 2043.

Scotland Gas Networks plc and Southern Gas Networks plc debt instruments are unsecured, while MidCo's debt instruments are secured, and all are stated after the deduction of unamortised issue costs of £15.4m (2022: £16.1m). These costs together with the interest expense are allocated to the profit and loss account over the term of the debt. Interest is calculated using the effective interest rate method.

Certain interest costs in respect of RPI- and CPI-linked debt are not payable until the principal amount of the loans are repaid and are included within the carrying value of the debt stated above. Certain interest costs in respect of CPI-linked swaps are also not payable until the maturity of the swap. The amount of interest in relation to the RPI- and CPI-linked debt included in the carrying value of the debt at 31 March 2023 is £392.9m (2022: £384.2m) and £10.0m (2022: £nil) respectively. The amount in relation to the CPI-linked swaps included in the carrying value of the debt at 31 March 2023 is £106.2m (2022: £35.6m).

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21. Financial instruments and risk management

In the normal course of business, the Group is exposed to financial risks including, but not limited to, market, credit and liquidity risk. This note explains the Group's exposure to these risks, how they are measured and assessed, and summarises the policies and processes used to manage them.

The Group operates a centralised treasury function which is responsible for the management of financial risks of the Group as a whole and each of the regulated entities on a standalone basis. Financial risks comprise exposure to funding risk, liquidity risk, counterparty credit risk, interest rate risk, inflation risk, credit spread risk and foreign exchange risk. The treasury function does not operate as a profit centre, nor does it enter into speculative transactions.

The Group's treasury activities are overseen by the Finance Committee, which meets on a periodic basis throughout the financial year. The Finance Committee comprises four Directors (one from each of the Group's shareholders) plus one statutory independent Non-Executive Director. The Group's Treasurer reports on a regular basis to the Finance Committee.

The Board reviews and approves all major treasury decisions.

Liquidity risk

Liquidity risk represents the risk of having insufficient funds to meet its financing in any particular subsidiary when needed.

To manage this risk the Group has a policy of actively maintaining a mixture of medium-term and long-term debt alongside committed facilities and short-term cash investments to ensure that the Group has sufficient available funds to meet forecast requirements over the short term to medium term. As part of their regulatory licence Scotland Gas Networks plc and Southern Gas Networks plc are required to submit an annual certificate to their Regulator, which includes a confirmation of sufficiency of financial resources (liquidity looking forward 12 months). The same principles are also applied across the wider Group.

To prevent over-reliance on individual sources of liquidity, funding is accessed across a range of instruments including: public bonds, bank loan facilities (including the RCF), private placements and EIB loans.

The Group currently has external financing (including undrawn revolving credit facilities) outstanding across four of the Group's subsidiaries:

- Scotia Gas Networks Limited: £356.3m shareholder loans;
- SGN MidCo Limited: £162.1m inflation-linked private placements; and £296.9m fixed rate private placements;
- Scotland Gas Networks plc: £473.6m fixed rate bonds; £79.7m floating rate bonds; £209.6m inflation-linked bonds; £457.7m fixed rate private placements; £100.0m EIB loans; £20.0m (undrawn) bank RCF; and £109.9m inflation-linked bank term loan facility; and
- Southern Gas Networks plc: £1,894.1m fixed rate bonds; £600.7m inflation-linked bonds; £355.6m fixed rate private placements; and £300.0m EIB loans; and £340.0m (undrawn) bank RCF.

Group subsidiaries are also funded through a combination of share capital, retained earnings and intercompany loans. Cash pooling structures are used to centralise surplus cash balances held by subsidiaries where possible to minimise external borrowings and interest costs. The treasury function seeks to minimise cash balances by conducting a detailed cash flow forecast process and timing funding issuance appropriately, however where surplus cash balances do arise these are invested in highly-rated bank deposits and money market funds.

As part of these processes the Group ensures that there is appropriate segregation between cash flows generated within the regulated businesses and those generated by other Group subsidiaries.

The contractual maturity of the Group's financial assets and liabilities are shown in the following tables. The amounts shown are gross cash inflows/(outflows) (including interest) with the exception of financial derivatives settled on a net basis where the amounts represent undiscounted net cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to relevant conditions existing at the reporting date.

2023

	0-6 months £m	6-12 months £m	1-2 years £m	2-5 years £m	> 5 years £m	Contractual cash flows £m	Interest/ discounting £m	Carrying value £m
Financial liabilities loans and borrowings								
Shareholder loans	(15.3)	(15.3)	(30.6)	(91.9)	(826.9)	(980.0)	623.7	(356.3)
Bank facility	–	–	–	–	–	–	–	–
Bonds	(63.7)	(402.1)	(537.1)	(1,441.8)	(4,371.5)	(6,816.2)	1,776.5	(5,039.7)
	(79.0)	(417.4)	(567.7)	(1,533.7)	(5,198.4)	(7,796.2)	2,400.2	(5,396.0)
Derivative financial liabilities								
Inflation-linked swaps	(10.1)	(12.1)	(22.4)	(69.0)	302.4	188.8	(261.8)	(73.0)
Interest rate swaps	0.9	0.7	1.5	5.7	34.2	43.0	(70.7)	(27.7)
Cross-currency swaps	1.2	3.6	7.2	21.7	162.7	196.4	(211.1)	(14.7)
	(8.0)	(7.8)	(13.7)	(41.6)	499.3	428.2	(543.6)	(115.4)
Other financial liabilities								
Trade creditors	(81.9)	–	–	–	–	(81.9)	–	(81.9)
Total financial liabilities	(168.9)	(425.2)	(581.4)	(1,575.3)	(4,699.1)	(7,449.9)	1,856.6	(5,593.3)

The Group expects to meet its obligations from cash balances, operating cash flows and refinancing.

The corresponding amounts for 2022 were as follows:

2022

	0-6 months £m	6-12 months £m	1-2 years £m	2-5 years £m	> 5 years £m	Contractual cash flows £m	Interest/ discounting £m	Carrying value £m
Financial liabilities loans and borrowings								
Shareholder loans	(15.3)	(15.3)	(30.6)	(91.9)	(857.5)	(1,010.6)	654.3	(356.3)
Bank facility	(30.0)	–	–	–	–	(30.0)	–	(30.0)
Bonds	(80.3)	(366.6)	(433.8)	(1,369.0)	(4,368.3)	(6,617.9)	1,823.9	(4,794.0)
	(125.6)	(381.9)	(464.4)	(1,460.9)	(5,225.8)	(7,658.5)	2,478.2	(5,180.3)
Derivative financial liabilities								
Inflation-linked swaps	(9.8)	(11.8)	(21.9)	(67.4)	250.9	140.0	(214.2)	(74.2)
Interest rate swaps	2.2	2.1	4.3	12.9	68.6	90.1	(146.8)	(56.7)
	(7.6)	(9.7)	(17.6)	(54.5)	319.5	230.1	(361.0)	(130.9)
Other financial liabilities								
Trade creditors	(54.9)	–	–	–	–	(54.9)	–	(54.9)
Total financial liabilities	(188.1)	(391.6)	(482.0)	(1,515.4)	(4,906.3)	(7,483.3)	2,117.2	(5,366.1)

Credit risk

Credit risk represents the risk that a counterparty does not settle an obligation for full value when that amount becomes due.

The Group is primarily exposed to credit risk arising from the extension of credit to its customers, cash deposits, derivatives and amounts due from external financing counterparties arising on certain committed facilities and financial instruments.

The maximum exposure to credit risk is the carrying value of financial assets as follows:

	2023 £m	2022 £m
Net trade receivables	**134.6**	119.8
Accrued income	**40.1**	34.8
Other debtors	**3.5**	2.3
Short term deposits	**245.9**	95.5
Cash	**43.3**	27.1
	467.4	279.5

21. Financial instruments and risk management (continued)

Trade and other receivables:
Our principal debtor exposure is governed by the credit rules within the Uniform Network Code. This sets out the level of credit relative to the RAV for each credit rating. Our credit policies and practices are designed to limit credit exposure by collecting security deposits prior to providing utility services, or after utility service has commenced if certain applicable regulatory requirements are met. Collection activities are managed daily. The utilisation of credit limits is regularly monitored and collateral is collected against these accounts when necessary.

Trade debtors 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. The Group contracts with shippers having investment grade ratings only, or where suitable collateral or cash prepayments are made. The Group currently holds £30.5m of security in respect of its trade counterparties (2022: £18.3m). These are included in trade creditors as at the year end.

Trade debtors from non-transportation income relates to consumers and businesses in relation to works for alterations, diversions, meters or damage repairs. In the year ending 31 March 2023 non-transportation debtors (£40.0m) were 29.7% (2022: 41.7%) of net trade debtors (£134.6m). An impairment allowance of £8.2m (2022: 8.7m) has been set aside according to the Group's impairment policy.

The largest transportation debtor is £19.2m (2022: £20.0m). There is no material credit exposure to any one customer.

The ageing of trade debtors net of impairment allowance is:

	2023 £m	2022 £m
Not past due	**125.6**	94.6
Past due 0-30 days	**0.1**	14.9
Past due 31-90 days	**0.6**	1.1
Past due over 90 days	**8.3**	9.2
	134.6	119.8

The maximum exposure to credit risk at the reporting date is the fair value of each class of debtors mentioned above.

At the end of each reporting year a review of the provision for bad and doubtful debts is performed taking into account the age, status and risk of recovery for each debtor.

Financial instruments:
The Group seeks to minimise its exposure to counterparties under financial instruments by agreeing individual exposure limits with the Finance Committee for financial instruments (based on instrument types and counterparty credit ratings) and by diversifying exposure across a range of counterparties. Counterparty credit ratings are monitored by the treasury function on a regular basis and ISDA agreements are in place with all counterparties to permit net settlement of assets and liabilities across certain financial instruments.

Counterparty credit risk arising from financial derivatives are managed through the maintenance of financial limits according to defined criteria, subject to a minimum credit rating of A-/A3 for new transactions and at credit ratings below this level counterparties are required to cash post collateral for mark to market positions owed to the regulated businesses within the Group. Investments of cash through deposits in the short term are also subject to review and approval according to defined criteria agreed by the Finance Committee and Board.

The Group conducted a review of counterparty credit risk and its own credit risk, and concluded that an adjustment was required to reflect the net credit risk in arriving at the fair value of financial instruments stated in the balance sheet. The net credit risk adjustment reduced liabilities by £36.2m (2022: £31.9m). The net credit risk adjustment related to inflation-linked swaps, interest rate swaps and cross-currency swaps. £29.3m (2022: £31.9m) was credited to the consolidated profit and loss account in the line 'Fair value movements on derivatives' and £6.9m (2022: £nil) was credited to other comprehensive income. The net credit risk adjustment was debited to 'Derivative financial liabilities' within 'Creditors: amounts falling due after more than one year' as presented in the consolidated balance sheet.

The net credit risk adjustment represents the risk of non-performance (or default) of either the counterparty or the Group in relation to financial instruments that require fair value measurements. These adjustments are respectively called Credit Value Adjustments (CVA) and Debit Value Adjustments (DVA).

The Mark to Market (MtM) value is calculated using a discounted cash flow method, which discounts the contracted future cash flows of derivatives using a risk-free rate (SONIA). The valuation is subsequently adjusted for the default risk of both the bank counterparty and the SGN entity respectively, by applying the CVA and DVA (together the 'net credit risk adjustment').

The CVA and DVA are calculated by running two separate Monte Carlo simulations, based on the bilateral credit risk adjustment method. Quoted credit default swap (CDS) spreads are used to determine counterparty credit curves when calculating the CVA. Z-spreads of senior unsecured public bonds are used to construct a credit curve for the Group when calculating the DVA. The net credit risk adjustment is made up of a CVA of £3.4m (2022: £1.9m) and a DVA of £(39.5)m (2022: £(33.8)m). The magnitude of the DVA adjustment as at 31 March 2023 is mainly due to the asymmetric cash flow positions. SGN settles the inflation accretion to the counterparty at maturity on the swap, whereas the Group receive cash flows from the counterparty at every interest rate settlement date (every six months) through to maturity. The inflation linked swaps are long dated with tenors of between 10 to 15 years, exacerbating the impact of the asymmetric cash flow position.

Market risk
Market risk represents the risk of losses or other adverse effects resulting from adverse changes in market prices or from unfavourable market conditions.

The Group is primarily exposed to market risk on UK interest rate; UK inflation rates and credit spreads in general.

Interest rate risk:
The Group's interest rate risk arises as a result of two primary sources:

- The mechanisms that the regulators have implemented to determine revenues for the Group's regulated businesses; and
- New and existing borrowings and financial instruments net of cash and cash equivalents, with the primary exposures arising from fluctuations in Sterling interest rates.

Certain of the Group's financing arrangements carry requirements to maintain exposure to fixed interest rates or inflation-linked above a certain level/within a range.

The Group manages its exposure to interest rate risk by targeting issuance in the most efficient markets available to achieve desired size and duration and using derivative financial instruments to manage the ultimate exposure to fixed/floating interest rates if required. In addition, the Group aims to maintain a smooth maturity profile across all debt instrument to ensure that there is no significant concentration of interest rate exposure when refinancing maturing debt.

The following table represents the annualised impact (net of deferred tax) of 100 basis point change in short-term interest rates at the reporting date in relation to equity and profit and loss account. The analysis assumes that all other variables remain constant.

	2023 £m	2022 £m
Impact on profit and loss account		
Floating rate instruments	**(4.5)**	(3.9)
Fixed to floating swaps	**(0.9)**	–
Floating to fixed swaps	**0.3**	–
	(5.1)	(3.9)
Impact on equity		
Floating to fixed swaps	**0.8**	0.8

Inflation risk:
The Group's inflation risk arises as a result of three primary sources:

- The mechanisms that the regulators have implemented to determine revenues for the Group's regulated businesses;
- Impact on controllable and non-controllable costs; and
- New and existing borrowings and financial instruments net of cash and cash equivalents, with the primary exposures arising from fluctuations in UK CPIH, CPI and RPI.

Certain of the Group's financing arrangements carry requirements to maintain exposure to fixed interest rates or inflation-linked above a certain level/within a range.

The Group manages its exposure to inflation rate risk by targeting issuance in the most efficient markets available to achieve desired size and duration and using derivative financial instruments to manage the ultimate exposure to inflation if required.

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21. Financial instruments and risk management (continued)

Certain of the Group's inflation-linked borrowings and financial instruments, including interest liabilities are exposed to a risk of changes in the carrying value due to changes in the UK Retail Price Index (RPI) and UK Consumer Price Index (CPI). The movements in these forms of liability offer a correlation to the movements in the Group's regulatory asset value which in the RIIO-GD2 price control is linked to CPIH due to the pricing mechanism imposed by the Regulator. The turnover capacity charges are also linked to CPIH. There is currently limited capacity in capital and financial markets to provide borrowings or financial instruments that are linked to CPIH.

By matching liabilities and assets in this way, inflation-linked borrowings and financial instruments partially hedge the exposure to changes in inflation.

The following table shows the illustrative effect on the profit and loss account that would result from a 1% movement in CPIH, CPI and RPI before the effects of tax.

	2023 £m	2022 £m
Impact on profit and loss		
Inflation-linked bonds	11.0	17.2
Inflation-linked swaps	7.7	–
Transportation income	(12.4)	(10.1)
Total	6.3	7.1

Credit spread risk:
The Group's credit spread risk arises as a result of the capital structure that is maintained, currently with external committed debt and facilities totalling £5,546.6m (including undrawn bank facilities but excluding shareholder loans and gross of unamortised issue costs). Lenders and investors assess the credit quality of the borrowing entity and charge a spread above benchmark rates to determine the overall return they require (and as a result the interest rate that the borrowing entity pays). Credit spreads can be impacted by both the specific credit risk of the borrower and macro events as well as general investor appetite for debt investments.

The Group manages its exposure to credit spreads by maintaining access to a diversified range of debt markets so that there is less exposure to a single group of investors/lender. The Group also maintains credit ratings with Fitch, Moody's and Standard & Poor's (S&P), with regular meetings and dialogue to support their appraisal, which ensures that a clear independent indication of the Group's credit risk is available to investors. In addition, the Group aims to maintain a smooth maturity profile across all debt instrument to ensure that there is no significant concentration of credit spread exposure when refinancing maturing debt.

Foreign exchange risk – transaction:
The Group is exposed to movements in foreign exchange rates due to its commercial trading transactions, however the volume of foreign denominated payments and receivables is not considered material and no active hedging of foreign exchange transactions is undertaken.

Foreign exchange risk – translation:
The Group seeks to match the currency of borrowings to the currency of its underlying investments. As the Group's assets are materially denominated in Sterling the Group and its subsidiaries seek to source Sterling debt. Debt is sourced from the most appropriate market or markets available at the time of raising new finance (including foreign currency markets) and appropriate derivative financial instruments transacted to manage the proceeds into the appropriate currency. In the last financial year, the Group issued USD denominated private placement notes that it fully hedged back to Sterling at issuance using cross-currency swaps. The Group has also issued private placement notes in the US that are denominated in Sterling where the underlying exposure is USD. On these transactions the noteholder has transacted a derivative financial instrument to hedge the USD exposure into Sterling and as a result the Group does not have exposure to USD under the transactions.

Cash flow hedges
Cash flow hedges comprise a floating to fixed interest rate swap at Scotland Gas Networks plc, hedging future floating rate interest payments on a floating rate bond, and cross-currency swaps put in place at Southern Gas Networks plc to fully hedge the principal and interest payments on certain USD denominated private placement notes. Receipts and payments for the swaps and the underlying bonds are exactly matched and in accordance with IAS 39 any gain or loss that is deferred to equity is recognised in profit or loss over the period that the floating rate interest payments impact on profit.

The interest rate swap at Scotland is in place to hedge future interest outflows on the floating rate bond and is therefore an effective hedging instrument.

The movement before deferred tax taken to the hedging reserve in equity in respect of this cash flow hedge in the year was a £26.9m gain (2022: £15.4m gain) and the ineffective portion of this hedge of £2.1m was credited to the profit and loss account (2022: £nil). The hedge reserve movement is expected to unwind in profit or loss over the life of the swaps. The notional principal amount of the outstanding cash flow hedges at 31 March 2023 was £80.0m (2022: £80.0m). As at 31 March 2023, the fixed rate of interest on this swap was 7.0575% and the floating rate was SONIA + 1.1193%. The uncompounded SONIA rate as at 31 March 2023 was 4.1777%.

Cross-currency swaps:
The movement before deferred tax taken to the profit and loss account in respect of cross-currency swaps in the year was a £14.7m loss (2022: £nil). The notional principal amount of the pay leg of the outstanding cross-currency swaps at 31 March 2023 amounted to £115.6m (2022: £nil), whilst the receive leg totalled $132m. As at 31 March 2023, the fixed rates of interest paid on these swaps were 6.2435%; 6.2585 and 6.2800%. The fixed rates of interest received were 5.63% and 5.73%.

Categories of financial instruments
The categories of financial assets and liabilities held by the Group were as follows:

	Book value	
	2023 £m	2022 £m
Financial assets held at amortised cost		
Trade debtors[1]	134.6	119.8
Short term deposits[1]	245.9	95.5
Other debtors	3.5	2.3
Cash	43.3	27.1
	427.3	244.7
Financial assets at fair value		
Derivative financial instruments – interest rate swaps	4.8	–
	4.8	–
Total financial assets	432.1	244.7

(1) The carrying amount of financial assets approximates to their fair value.

	Book value	
	2023 £m	2022 £m
Financial liabilities held at amortised cost		
Trade creditors	81.9	51.2
Accrued interest	56.4	51.5
Other accruals	134.7	108.6
Bank facility	-	30.0
Borrowings	5,039.7	4,794.0
Shareholder loans	356.3	356.3
	5,669.0	5,391.6
Financial liabilities at fair value		
Derivative financial instruments – inflation-linked swaps	73.0	74.2
Derivative financial instruments – interest rate swaps	27.7	56.7
Derivative financial instruments – cross-currency swaps	14.7	–
	115.4	130.9
Total financial liabilities	5,784.4	5,522.5

The carrying amount of financial liabilities approximates to their fair value except for bonds and shareholder loans, the fair value of which is disclosed on the next page.

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1: Valued using unadjusted quoted prices in active markets for identified financial instruments;
- Level 2: Valued using techniques based significantly on observable market data. Instruments in this category are valued using valuation techniques where all of the inputs that have a significant impact on the valuation are directly or indirectly based on observable market data;

21. Financial instruments and risk management (continued)

- Level 3: Instruments in this category have been valued using a valuation technique where at least one input (which has a significant input on the financial instruments' valuation) is not based on observable market data. Where inputs can be observed from market data with not undue cost and effort, the observed input is used. Otherwise management determines a reasonable estimate for the input.

An analysis of financial assets and liabilities that are recorded at fair value at 31 March 2023 is as follows:

2023	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets				
At fair value through profit and loss				
– Derivative financial instruments – interest rate swaps	–	4.8	–	4.8
	–	4.8	–	4.8
Financial liabilities				
At fair value through profit and loss				
– Derivative financial instruments – inflation-linked swaps	–	73.0	–	73.0
– Derivative financial instruments – interest rate swaps	–	27.7	–	27.7
– Derivative financial instruments – cross-currency swaps	–	14.7	–	14.7
	–	115.4	–	115.4

2022	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial liabilities				
At fair value through profit and loss				
– Financial derivatives – mirror swaps	–	74.2	–	74.2
Financial derivatives – hedging swaps	–	56.7	–	56.7
	–	130.9	–	130.9

Mirror swaps

In 2005 the Group entered into interest rate swap contracts to fix the Group'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 2022 the mirror swap loss was £nil.

In March 2022 both sides of the Group's mirror swaps were terminated with the mark to market value cash settled for a total consideration of £21.5m. The debit has been taken to the financial instruments' liability in the balance sheet and a difference of £0.9m between the carrying mark to market value of the swaps compared to the settlement value has been written off within the interest receivable and similar income line in the profit and loss account. This resulted in the elimination of any liability for the mirror swaps on the Group's balance sheet. The £21.5m cash settlement was recognised in the 'payments of mirror swaps' line of the cash flow statement, within cash flows from financing activities.

Inflation-linked swaps

In June 2022 the Group transacted £670m of CPI-linked swaps that economically convert some or all of the notional principal of the following existing fixed rate debt instruments into CPI-linked debt instruments:

- £150m fixed rate notes maturing in 2030;
- £250m fixed rate bond maturing in 2031;
- £130m fixed rate notes maturing in 2033;
- £100m fixed rate notes maturing in 2034; and
- £40m of the £400m fixed rate bond maturing in 2036.

Interest rate swaps

In October 2022, Scotland Gas Networks plc entered into three interest rate swaps totalling £90m that convert some or all of the £184m fixed rate notes, entered into within the same month, into floating rates based on SONIA:

- £30m of the £34m notes due 2032 converted from fixed to SONIA plus 2.115%, effective October 2022;
- £30m of the £30m notes due 2035 converted from fixed to SONIA plus 2.373%, effective March 2023;
- £30m of the £50m notes due 2035 converted from fixed to SONIA plus 2.2695%, effective October 2022.

In June 2022 the mandatory break on Scotland Gas Networks plc's £80m IRS was extended by 10 years to March 2033. As part of this exercise, the swap was novated to another of the Group's relationship banks and the fixed rate payable leg was increased by around 0.5%. The floating rate receivable was unchanged and remains the same as the floating rate payable on the hedged £80m floating rate bond due 2043.

In February 2023, Scotland Gas Networks plc entered into a single £30m interest rate swap to 're-fix' the interest rate swap hedging the fixed rate notes due in 2032. The new swap's floating receive leg exactly offsets the original swap's floating pay leg, resulting in a net fixed exposure.

Cross-currency swaps

In October 2022, Southern Gas Networks plc issued a total of $132m in private placement notes, for which drawing occurred in March 2023:

- $66m 5.63% fixed rate notes due 2033;
- $66m 5.73% fixed rate notes due 2035.

In line with the Company's hedging policy, the entire principal amounts and interest payments under these notes have been hedged using cross currency-swaps with effective dates matching the drawdown profiles of the notes. Under these cross-currency swaps, the Company receives a USD upfront payment and fixed USD payments equal to the principal amounts and coupons under the notes respectively, and pays fixed GBP amounts:

- $41m converted to £36m with fixed 6.2440% GBP interest payable, due 2033, effective March 2023;
- $25m converted to £22m with fixed 6.2485% GBP interest payable, due 2033, effective March 2023;
- $66m converted to £59m with fixed 6.2800% GBP interest payable, due 2035, effective March 2023.

Fair values

The Group's financial instruments recorded at amortised cost are shown below together with their fair values:

	31 March 2023		31 March 2022	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Borrowings	**5,039.7**	**5,240.4**	4,794.0	5,702.7
Bank facility	**–**	**–**	30.0	30.0
Shareholder loans	**356.3**	**458.5**	356.3	638.9
	5,396.0	**5,698.9**	5,180.3	6,371.6

Fair values of borrowings and shareholder loans have been determined by reference to closing quoted market values where available or otherwise by discounting future cash flows at their market interest rate.

The carrying value of all other financial assets and liabilities approximates to their book value.

22. Provisions for liabilities

	Environmental and demolition £m	Deferred tax £m	Other provisions £m	Total £m
Group				
At 1 April 2022	47.5	1,046.3	17.8	1,111.6
Reassessments during the year	(1.1)	–	31.1	30.0
Utilised during the year	(6.0)	–	(0.8)	(6.8)
Net movement in deferred tax	–	2.4	–	2.4
Amortisation of discount	1.6	–	0.1	1.7
At 31 March 2023	**42.0**	**1,048.7**	**48.2**	**1,138.9**

22. Provisions for liabilities (continued)

Environmental and demolition
The environmental provision represents the Directors' best estimate of environmental restoration costs, where the Group has a legal obligation to restore sites at the balance sheet date. The provision has been discounted at the nominal rate of 3.21% (2022: 1.45%) 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 three years in line with anticipated regulatory output requirements for land remediation.

The demolition provision is an obligation to demolish the gas holders on sites held in inventories. The provision is based on third-party valuations that have been discounted at the nominal rate of 3.21% (2022: 1.45%) to the present value of the estimated expenditure to settle the obligation. They are expected to be utilised over the next three years.

Deferred tax
The net movement on the deferred tax provision has arisen mainly as a result of movements in the defined benefit pension asset, offset by other movements in the year of which £26.4m (2022: £224.0m) is recorded as a debit (2022: debit) to the profit and loss account and £24.0m (2022: £19.0m) is recorded as a gain (2022: gain) to the statement of comprehensive income.

Deferred tax recognised in the financial statements is as follows:

	Group		Company	
	2023 £m	2022 £m	**2023 £m**	2022 £m
Accelerated capital allowances	**(994.9)**	(990.7)	**-**	–
Deferred tax on cash flow hedges	**6.9**	14.2	**-**	–
Deferred tax on inflation-linked swaps	**(5.8)**	9.6	**-**	–
Deferred tax on defined pension benefits	**(61.5)**	(90.7)	**-**	–
Other timing differences	**6.6**	11.3	**-**	6.0
	(1,048.7)	(1,046.3)	**-**	6.0

Other timing differences relate to elimination of intergroup profits and the unwinding of discount on provisions.

Movements in deferred tax take into account the effects of changes in the fair value liability of the Company's inflation-linked swap portfolio. Increases or reductions in the fair value liability of the Company's inflation linked swap portfolio represent an increase or reduction in the net interest the financial markets expect will be payable on those inflation-linked swaps in future years. Changes to the fair value of the liability are not tax deductible under UK tax regulations as tax deductions are only available as and when the future interest payments are actually paid. The increase in the fair value of the inflation-linked swap portfolio will therefore create an accounting cost which is not subject to taxation until the interest is paid and therefore creates a timing difference. The fair value of the inflation-linked swap portfolio can fluctuate significantly and there will be a consequential impact on the deferred tax provision.

Amounts not recognised relate to the corporate interest restriction. Due to an election made during the year, the Group no longer has the ability to utilise deferred tax assets on restricted interest expenditure against existing deferred tax liabilities.

The movement in provision for deferred tax is as follows:

	Group	
	2023 £m	2022 £m
At 1 April	**(1,046.3)**	(803.3)
Debited to profit and loss account	**(26.4)**	(224.0)
Credited/(charged) to other comprehensive income	**24.0**	(19.0)
At 31 March	**(1,048.7)**	(1,046.3)

The Group is not expecting a reversal of deferred tax in the next financial year.

The Group has not recognised deferred tax assets in respect of £235.0m (2022: £235.0m) of unutilised tax losses, £67.0m (2022: £67.0m) of capital losses and £85.3m (2022: £29.6m) of corporate interest restriction disallowances. These assets have not been recognised as the Group is uncertain that there will be sufficient future taxable profits against which to utilise the assets. 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 note 10 to the financial statements).

The Company has not recognised deferred tax on £235.0m (2022: £235.0m) of unutilised tax losses.

Other provisions
Other provisions consist of asbestos related liabilities and other provisions relating to the operations of our gas networks, including the Operational target provision, detailed in note 2. The other provisions represent management's best estimates of the future expenditure necessary to settle the obligations. The provision has been discounted and is stated at the present value of the estimated expenditure to settle the obligation. The asbestos related provision is expected to be utilised over the next 29 years. The other provisions relating to the operations of our gas networks are expected to be utilised in the next 2 years.

During the year, an onerous contract has been identified in relation to the H100 Fife project, as a result of cost overruns. The onerous provision of £15.9m (2022: £nil) reflects the unavoidable costs under the contract, which are the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. The provision represents management's best estimates of the future expenditure necessary to settle the obligations.

The Company has £0.1m (2022: £nil) of other provisions for redundancies.

23. Deferred income

Group	Connections £m	Replacement £m	Other £m	**Total 2023 £m**	Total 2022 £m
Customer contributions					
Customer contributions brought forward	276.1	187.4	0.8	464.3	438.0
Customer contributions deferred in the year	19.0	14.0	–	33.0	37.0
Amortisation in year	(7.7)	(3.6)	–	(11.3)	(10.7)
Utilised in the year	–	–	(0.8)	(0.8)	–
Total customer contributions	**287.4**	**197.8**	**-**	**485.2**	**464.3**
Government grants					
Government grants brought forward	–	–	6.9	6.9	6.9
Government grants amortisation	–	–	(0.4)	(0.4)	–
Government grants utilised in the year	–	–	(0.8)	(0.8)	–
Total government grants	**-**	**-**	**5.7**	**5.7**	**6.9**
Total deferred income	**287.4**	**197.8**	**5.7**	**490.9**	**471.2**

The Group has received customer contributions relating to plant and machinery. In accordance with the Group'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.

Other deferred income relates to contributions received from fellow gas distribution networks and the Scottish Government towards the funding of the Group's H100 Fife project.

The Company has no deferred income.

24. Share capital

	31 March 2023		31 March 2022	
	Number	**Value £m**	Number	Value £m
Allotted, called up and fully paid shares				
'A' ordinary shares of 42.55p (2022: 42.55p) each	**235,025,002**	**100.0**	235,025,002	100.0
'B' ordinary shares of 42.55p (2022: 42.55p) each	**117,512,501**	**50.0**	117,512,501	50.0
'C' ordinary shares of 42.55p (2022: 42.55p) each	**117,512,501**	**50.0**	117,512,501	50.0
Total	**470,050,004**	**200.0**	470,050,004	200.0

The 'A', 'B' and 'C' ordinary shares rank pari passu in all respects.

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for the year ended 31 March 2023

25. Reconciliation of movements in Group shareholders' funds

	2023 £m	2022 £m
Profit/(loss) for the financial year	**95.2**	(187.2)
Dividend paid on equity shares (see note 12)	**(54.5)**	(84.0)
Cash flow hedges (net of deferred tax)	**15.7**	16.1
Actuarial (loss)/gain on defined benefit pension scheme (net of related deferred tax)	**(87.8)**	37.5
Movement in shareholders' funds	**(31.4)**	(217.6)
Opening shareholders' funds	**881.7**	1,099.3
Closing shareholders' funds	**850.3**	881.7

26. Operating lease commitments

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

	Other		Land and buildings	
	2023 £m	2022 £m	2023 £m	2022 £m
Within one year	**2.2**	2.2	**2.0**	1.0
Within two to five years	**2.8**	3.3	**7.7**	3.7
After five years	**–**	–	**21.5**	14.4
Total	**5.0**	5.5	**31.2**	19.1

The Company has no operating lease commitments in either year.

27. Commitments and contingencies

Capital commitments
Capital projects contracted for by the Group but not provided in the financial statements amounted to £51.6m at 31 March 2023 (2022: £32.8m). The Company has capital commitments of £nil at 31 March 2023 (2022: £nil).

Contingent liabilities
Through the ordinary course of operations, the Company is party to various litigation, claims and investigations.

In relation to the incident at Galpin's Road on 8 August 2022, the Group is continuing to support the police and Health and Safety Executive with their investigation. Due to the early stage of the investigation, it is not possible for management to reliably estimate the financial impact or timing of any future obligation as at 31 March 2023.

28. Pension commitments

A significant proportion of the Group's employees are members of the Scotia Gas Networks Pension Scheme ('the Scheme'). 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. The Scheme provides final salary defined benefits for employees who joined the Lattice Group Scheme prior to 31 March 2002. A defined contribution section was added to the Lattice Group Scheme from 1 April 2002 for employees joining the Lattice Group Scheme from that date. Employees of the Group who were previously members of the Lattice Group Scheme transferred to the Scotia Gas Networks Pension Scheme on 1 December 2005.

a) Defined Benefit Scheme
The Scheme is operated by the Group and is funded with assets held in separate trustee administered funds. It is subject to independent valuations at least every three years, on the basis of which the qualified actuary determines the rate of employers' contribution, which, together with the specified contributions payable by the employees and proceeds from the Scheme's assets, are expected to be sufficient to fund the benefits payable under the Scheme.

The most recent triennial valuation of the Scheme was carried out at 31 March 2021. 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 Broadstone Corporate Benefits Limited at 31 March 2023 using the projected unit method.

The following financial assumptions have been used:

	2023	2022	2021	2020
As at 31 March				
Discount rate	**4.65%**	2.75%	2.0%	2.3%
Retail price inflation	**3.50%**	3.75%	3.5%	2.8%
Consumer price inflation	**3.10%**	3.35%	3.1%	1.8%
Rate of increase of salaries	**3.30%**	3.55%	3.3%	2.6%
Rate of increase of pensions payment	**3.50%**	3.75%	3.5%	2.8%

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 expectancy in years for a member once they reach age 65 is as follows:

	2023		2022		2021	
	Male	Female	Male	Female	Male	Female
As at 31 March						
Members currently aged 65	**22.3**	**24.7**	22.8	24.4	22.7	24.3
Members currently aged 45	**24.3**	**26.8**	24.5	27.0	24.4	26.9

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

	Sensitivity	Approximate change in DBO £000
Discount rate	– 0.1% p.a.	9.3
	+ 0.1% p.a.	(9.1)
Price inflation (RPI measure) (1)	– 0.1% p.a.	(8.8)
	+ 0.1% p.a.	8.5
Life expectancy	– 1 year	(24.6)
	+ 1 year	25.7

(1) These movements have been calculated assuming that changes in the inflation assumption affect all inflation linked assumptions.

The fair value of the assets in the scheme and the present value of the liabilities in the scheme were:

As at 31 March

	2023			2022		
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equities	**–**	**–**	**–**	126.5	–	126.5
Government bonds (1)	**404.1**	**–**	**404.1**	535.2	–	535.2
Corporate bonds	**136.4**	**103.4**	**239.8**	189.8	110.3	300.1
Property	**–**	**0.1**	**0.1**	–	1.1	1.1
Cash	**–**	**10.8**	**10.8**	–	11.0	11.0
Insurance contracts	**–**	**198.6**	**198.6**	–	247.3	247.3
Total market value of assets	**540.5**	**312.9**	**853.4**	851.5	369.7	1,221.2
Actuarial value of liabilities			**(607.4)**			(858.7)
Surplus in scheme			**246.0**			362.5

(1) Including LDI repurchase agreement liabilities.

The fair value of scheme assets at 31 March 2023 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.

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for the year ended 31 March 2023

28. Pension commitments (continued)

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 contributes to overall hedging levels for the Scheme of 95% for interest rates and 95% for inflation as at 31 March 2023 with respect to the pension scheme liabilities of £0.6bn (valued using the UK Government bond yield curve). These LDI assets, which provide both interest rate and inflation protection, are managed by BlackRock and include a variety of instruments, including UK Government bonds (gilts), interest rate swaps, inflation swaps, gilt repos and corporate bonds. Further interest rate protection is provided by investment grade credit funds, including those managed by BlackRock and Goldman Sachs. The Scheme has also implemented pensioner buy-ins which contribute to the total interest rate hedging ratios referred to above.

After considering the Scheme's strong funding level and the advice of the Scheme's investment advisors, in March 2023 the Scheme's trustees agreed to undertake some further de-risking of the investment portfolio and fully sell out of all equity positions. The proceeds of the sale were invested into LDI assets initially, with a longer-term investment strategy for the proceeds to be agreed by the Trustees over the course of the 2023/24 financial year.

Movement in fair value of Scheme assets

	2023 £m	2022 £m
At 1 April	1,221.2	1,236.0
Interest income	33.4	24.5
Contributions from the Group	7.7	20.9
Remeasurement of Scheme assets	(369.3)	(15.8)
Benefits paid	(38.3)	(42.7)
Administration costs	(1.3)	(1.7)
As at 31 March	853.4	1,221.2

Movement in fair value of Scheme liabilities

	2023 £m	2022 £m
At 1 April	(858.7)	(937.3)
Current service cost	(15.9)	(18.5)
Past service cost	-	–
Interest cost	(23.3)	(18.5)
Actuarial gains	252.2	72.9
Benefits paid	38.3	42.7
At 31 March	(607.4)	(858.7)

Employer contributions for the period ending 31 March 2023 were 37.3% (2022: 37.3%) of monthly salary roll, before allowing for any salary sacrifice contributions. Deficit contributions were not payable from 1 April 2022 (2022: £12.5m p.a. from 1 April 2021 to 31 March 2022).

The actual (loss)/return on plan assets was:

	2023 £m	2022 £m
Loss on plan assets excluding interest income	(369.3)	(15.8)
Interest income on plan assets	33.4	24.5
Actual (loss)/return on plan assets	(335.9)	8.7

The cumulative amount of actuarial gains recognised in the statement of comprehensive income since adoption total £272.5m (2022: £20.3m).

Analysis of the amounts recognised in the profit and loss account

	2023 £m	2022 £m
Amount charged to net operating costs:		
Current service cost	(15.9)	(18.5)
Administration cost	(1.3)	(1.7)
Total charge to net operating costs	(17.2)	(20.2)
Analysis of the amount credited/(charged) to finance income/expense:		
Interest income on pension scheme assets	33.4	24.5
Interest cost on pension scheme liabilities	(23.3)	(18.5)
Net finance income	10.1	6.0
Net charge to the profit and loss account	(7.1)	(14.2)

Analysis of the amount recognised in other comprehensive income

	2023 £m	2022 £m
Actual loss on scheme assets	(369.3)	(15.8)
Actuarial gains on scheme liabilities	252.2	72.9
(Loss)/gain recognised in other comprehensive income	(117.1)	57.1

b) Defined contribution schemes

The amounts recognised in the profit and loss account are as follows:

	2023 £m	2022 £m
Amount charged in respect of defined contribution schemes	19.9	17.2

29. Related parties

The Company is owned by Apple Newco Limited (37.5%) which is indirectly wholly-owned by Ontario Teachers' Pension Plan Board, UK Gas Distribution 2 Limited (37.5%), which is indirectly owned by Brookfield Super-Core Infrastructure Partners, and Speyside Bidco Limited (25.0%) which is wholly-owned by funds managed by Global Infrastructure Partners (GIP).

It is the opinion of the Directors that the Group and Company have no single controlling party.

Transactions with key management personnel

Total compensation of key management personnel in the year amounted to £6.4m (2022: £5.1m). Directors are also deemed to be key management personnel and their remuneration is disclosed in note 7.

Transactions with shareholders

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

	Group	
	2023 £m	2022 £m
Shareholders' loans:		
UK Gas Distribution 2 Limited	133.6	133.6
Speyside Bidco Limited	89.1	89.1
Apple Newco Limited	133.6	133.6
	356.3	356.3
Interest owed to shareholders:		
UK Gas Distribution 2 Limited	3.8	3.9
Speyside Bidco Limited	2.6	2.5
Apple Newco Limited	3.8	3.9
	10.2	10.3

The aggregate interest expense charged to the profit and loss account in respect of shareholders' loans was £30.6m (2022: £30.7m). Interest accrues on the shareholders' loans at a fixed rate of 8.6% per annum and is payable semi-annually in arrears on 30 November and 31 May each year. The Company may, upon giving due notice, elect to pay some or all of the interest payable through the issuance of further loans to its shareholders.

Notes to the financial statements

for the year ended 31 March 2023

29. Related parties (continued)

During the year ended 31 March 2022, the Company underwent an ownership change and as such SSE plc ceased to be a shareholder and related party. Other than interest charges relating to shareholder loans, the following transactions took place during the previous year between the Group and the SSE plc group of companies (SSE).

	2023 £m	2022 £m
Sales of goods and services	-	10.1
Purchase of goods and services	-	(43.0)

Sales of goods and services to SSE primarily represent gas transportation services. At 31 March 2022 an amount of £nil was owed by SSE in relation to these services.

Transactions with other related parties

In the year the Group also invested £1.5m in a Joint Venture, Murphy Asset Services Limited (2022: £4.2m). The Group also accounted for a share of the loss to the year ended 31 March 2023 of £1.0m (2022: £1.4m).

The Company contributed £7.7m (2022: £20.9m) to Scotia Gas Networks Pension Scheme during the year.

30. Analysis of changes in net debt

Analysis of changes in net debt	2022 £m	Cash flow £m	Other non-cash movements £m	2023 £m
Net cash and cash equivalents				
Cash at bank	27.1	16.2	–	**43.3**
Short term deposits	95.5	150.4	–	**245.9**
	122.6	166.6	–	**289.2**
Financial liabilities, loans and borrowings				
Debt due within one year (note 19)	(296.2)	308.7	(312.3)	**(299.8)**
Debt due after one year (note 20)	(5,089.3)	(399.0)	392.1	**(5,096.2)**
	(5,385.5)	(90.3)	79.8	**(5,396.0)**
Derivative financial instruments	(130.9)	–	20.3	**(110.6)**
Total	(5,393.8)	76.3	100.1	**(5,217.4)**

Other non-cash movements in borrowings relate to the amortisation of borrowing fees, loan accretion accruals and foreign exchange variances.

Non-cash movements in derivative financial instruments relate to fair value movement and accretion accruals.

31. Other notes to the cash flow statement

In June 2022, the Group agreed to settle outstanding fees due in relation to certain guarantees provided by Assured Guarantee Corp. (as agent for Syncora Guarantee Inc.) and Assured Guarantee UK Limited that were previously in place over certain outstanding public bond instruments. The cash settlement amount of £9.2m is included within interest paid in the Consolidated Cash Flow Statement. In the prior year, included in interest paid was £4.3m in relation to the settlement of fees due to a prior guarantor of certain public bonds. Also included in prior year payments of mirror swaps was £21.5m in relation to the termination of the Group's mirror swaps.

32. Subsequent events

In May 2023, Scotland Gas Networks plc entered into a single £30m interest rate swap to 're-fix' the interest rate swap hedging the fixed rate notes due in 2035 that was effective in March 2023. The new swap's floating receive leg exactly offsets the original swap's floating pay leg, resulting in a net fixed exposure.

In June 2023, Southern Gas Networks plc entered into a £550m committed bridging loan with three of its relationship banks. The bridging loan has an initial tenor of 12 months and the Company has the option to extend it for a further six months thereafter. It has a floating drawn rate of interest based on SONIA plus a time-dependent margin. The bridge is intended to provide additional liquidity for Southern Gas Networks plc's refinancing requirements.

Alternative performance measures

When assessing and discussing the Group's reported financial performance, financial position and cash flows, management makes reference to Alternative Performance Measures (APMs) that are not defined or specified under UK GAAP.

APMs are presented to enhance the reader's evaluation of ongoing performance and to facilitate meaningful comparison of results between reporting periods. The APMs used in this report are consistently applied across reporting periods.

Management uses these APMs to evaluate ongoing operations and in reporting to investors and regulatory bodies.

Group APM	Closest equivalent UK GAAP measure	Adjustments to reconcile to primary statements	Rationale for adjustments
Cash flow after investing activities	Operating cash flow	Excluding interest paid and including net cash flow from investing activities.	Due to the nature of the business cash flow from core activities are considered to be operating activities and investment in our gas infrastructure.
Net debt to Regulated Asset Value (RAV)	Borrowings	Net debt (before issue costs) excluding shareholders' loans and liabilities arising from derivative financial instruments and net of cash and cash equivalents. RAV is as reported to Ofgem in the Regulatory Reporting Pack (RRP). This does not have a statutory equivalent.	Governed by specific licence conditions and covenants imposed on us due to the nature of the business.
Capital expenditure	Tangible and intangible fixed asset additions	Tangible and intangible fixed asset additions excluding replacement expenditure.	This is an Ofgem driven performance measure. Due to the nature of the business replacement expenditure is material to the financial statements and thus it should be disclosed separately.
Replacement expenditure	Tangible and intangible fixed asset additions	Tangible and intangible fixed asset additions excluding capital expenditure.	
Regulated Asset Value (RAV)	Tangible and intangible assets	RAV is as reported to Ofgem in the Regulatory Reporting Pack (RRP). This does not have a statutory equivalent.	Governed by specific licence conditions due to the nature of the business.

Glossary

AC – Audit Committee
ADIA – Abu Dhabi Investment Authority
AFS – Available-for-Sale
AGM – Annual General Meeting
AI – Artificial Intelligence
APMs – Alternative Performance Measures
AUSMOS – Automated Utility Service Mark-out System
CCUS – Carbon Capture, Usage and Storage
CDP – Carbon Disclosure Project
CDS – Credit Default Swap
CEO – Chief Executive Officer
CESC – Commercial Engineering & Safety Committee
CFO – Chief Financial Officer
CGUs – Cost Generating Units
CISBOT – A cast iron pipe-repair robot that seals joints in natural gas pipelines from the inside
CO – Carbon Monoxide
Consolidated MidCo group – Consists of SGN MidCo Ltd, Scotland Gas Networks plc, Southern Gas Networks plc, SGN Natural Gas Ltd, and SGN Contracting Ltd
Covid-19 – Coronavirus disease
CPI – Consumer Price Index
CPIH – Consumer Prices Index including owner occupiers' housing costs
CSE – Centre for Sustainable Energy
CSEG – Customer and Stakeholder Engagement Group
CVA – Credit Value Adjustment
Defra – Department for Environment Food & Rural Affairs
DNO – Distribution Network Operator
DVA – Debit Value Adjustment
EIB – European Investment Bank
EMEA – Europe, the Middle East and Africa
EMTN – Euro Medium-term Note Programme
ENA – Energy Networks Association
ESC – Engineering and Safety Committee
ESG – Environmental, Social and Governance
Executive/Executive Leadership Team – The CEO, CFO and department Directors
FC – Finance Committee
FIFO – First-in, First-out
FoEC – Future of Energy Committee
FPNES – Fuel Poor Network Extension Scheme
FRC – Financial Reporting Council
FRS 102 – The Financial Reporting Standard applicable in the UK and Republic of Ireland
FSB – Financial Stability Board
FVTPL – Fair Value Through Profit or Loss
FY – Financial Year
FYLD – Digital, mobile platform, using speech and image recognition
GAAP – Generally Accepted Accounting Principles
GB – Great Britain
GCC – Gas Control Centre
GDN – Gas Distribution Network
GIP – Global Infrastructure Partners
GP – General Practitioner
GPR – Ground Penetrating Radar
GWh – Gigawatt hour
HMRC – His Majesty's Revenue and Customs
HP – High Pressure
HR – Human Resources
HSC – Health & Safety Committee
HSE – Health and Safety Executive
I&C – Industrial and Commercial
IP – Intermediate Pressure
IT – Information Technology
JV – Joint Venture
KPI – Key Performance Indicator
LDI – Liability Driven Investment
LNG – Liquefied Natural Gas
LP – Low Pressure
LTIP – Long-term Incentive Plan
LTS – Local Transmission System
ML – Machine Learning
MSA – Managed Service Agreement
MtM – Mark to Market
MUA – Murphy Utility Assets
NIAUR – Northern Ireland Authority Utility Regulation
NIS – Network and Information Systems
NomCo – Nomination Committee
OBE – Order of the British Empire
Ofgem – Office of Gas and Electricity Markets Ofgem is responsible for regulating the gas and electricity markets in the UK to ensure customers' interests are protected
OMERS – Ontario Municipal Employees' Retirement System
OT – Operational Technology
OTPPB – Ontario Teachers' Pension Plan Board
PAYE – Pay As You Earn
PE – Polyethylene
PSR – Priority Services Register
R&D – Research and Development
RAV – Regulated Asset Value
RCF – Revolving Credit Facility
Regulated businesses – Consists of Scotland Gas Networks plc, Southern Gas Networks plc, and SGN Natural Gas Ltd
RemCo – Remuneration Committee
RIC – Regulatory Investment Committee
RIDDOR – Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2013
RIIO-GD2 – The current price control period that runs from 1 April 2021 to 31 March 2026
RIIO-GD3 – The price control period that will run from 1 April 2026
RPI – Retail Price Index
RRP – Regulatory Reporting Pack
RTC – Road Traffic Collision
SESG – Stakeholder, Environment, Social & Governance Committee
S&Ps – Standard and Poor's
ScGN – Scotland Gas Networks plc
SDGs – Sustainable Development Goals
SECR – Streamlined Energy and Carbon Reporting
SESG – Stakeholder, Environment, Social & Governance Committee
SID – Sufficiently Independent Director
SIF – Strategic Innovation Fund
SIUs – Scottish Independent Undertakings
SoGN – Southern Gas Networks plc
SoLR – Supplier of Last Resort
SONIA – Sterling Overnight Index Average
SRM – Supplier Relationship Management
SSE – Scottish and Southern Electricity
STIP – Short-term Incentive Plan
TCFD – Task Force on Climate-related Financial Disclosures
tCO_2e – Tonnes of CO_2e
The Group – The Company and its subsidiary undertakings (together the Group)
TNI – Total Network Investment
TWh – Terawatt hour
UN – United Nations
UREGNI – Utility Regulator for Northern Ireland
USD – United States Dollar
Vac ex – Vacuum excavation
VCMA – Vulnerability and Carbon Monoxide Allowance
WASH – Warm and Safe Homes Advice Service
WEF – World Economic Forum

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If you smell gas or are worried about gas safety you can call the National Gas Emergency Number on **0800 111 999**

Carbon monoxide (CO) can kill. For more information visit **sgn.co.uk/help-and-advice**