Company registration number: 10615396

Quadgas MidCo Limited

Annual Report and Financial Statements

For the year ended 31 March 2020

Quadgas MidCo Limited

Strategic Report

For the year ended 31 March 2020

The Directors present their Report and the audited financial statements of the Group and the company for the year ended 31 March 2020.

Principal activities

Quadgas MidCo Limited (the company) holds investments in a number of subsidiary companies and obtains and provides finance to fellow subsidiary companies via intercompany transactions.

The Group comprises Quadgas MidCo Limited, Quadgas Finance Plc, Cadent Services Limited, Cadent Finance Plc, Cadent Gas Limited, Cadent Gas Pension Trustee Limited, Cadent Gas Pension Property Company 1 Limited, Cadent Gas Pension Property Company 2 Limited and Cadent Gas Pension Services Limited. Cadent Gas Limited is the main trading company and operates four of the eight regional gas distribution networks in Great Britain. Using the Group's network, approximately 40 gas shippers and suppliers transport gas to 11 million homes and businesses. Cadent Gas also manages the national gas emergency service free phone line, taking calls and giving safety advice on behalf of the UK gas industry.

Strategy

The Group’s strategy is to set new standards on the quality of the services we deliver to all of our customers (our consumers, suppliers and shippers), stakeholders and communities, particularly those that find themselves in vulnerable situations. We have developed a customer first approach that has an ethos of constantly maintaining availability of gas supplies to our customers by developing appropriate techniques and using innovative ways to achieve this goal. We will also push the boundaries on our role in supporting safety of customers in the home, helping alleviate fuel poverty and making our services more accessible to all types of customer.

Future developments

The debate about the future of gas has been rapidly climbing up the political agenda. As the UK’s largest gas distribution company by a considerable margin, it is natural that Cadent should take a role as a leading voice for the industry.

Gas currently powers around 80% of homes in the UK and clean gas has a crucial role to play in the future energy mix as we transition towards a low-carbon future. At the start of 2020, Cadent became the first gas distribution network in the UK to deliver hydrogen to homes through our HyDeploy project. This marks a major step towards proving the case for the future use of hydrogen. We are also developing an extensive project to introduce a hydrogen blend into a much larger part of the network with HyNet in the North West. This complex and ambitious project will make a significant contribution to reducing carbon and will show what can be achieved by using large-scale hydrogen production to support decarbonisation in a cost-effective way. We will continue to engage with Government and regulators to build awareness of the opportunities offered by clean gas as we support the journey towards Net Zero.

In early 2020, the spread of coronavirus 'COVID-19' caused huge change to daily life in the UK and across the world. By nature of its operating business, the company has not been significantly impacted and the Directors believe the current level of trading activity as reported in the income statement will continue in the foreseeable future with no anticipated significant movements in the statement of financial position. See page 3 for our detailed assessment.

Business environment
The Group manages the gas distribution networks to keep the gas flowing safely and reliably to help keep our 11 million customers connected, safe and warm. The Group are incentivised through Ofgem's regulatory framework called RIIO (Revenue = Incentives + Innovation + Output) to operate efficiently and deliver services that our customers and stakeholders value. These are expressed as output commitments across six key categories (safety, reliability, environment, social obligations, customer satisfaction and facilitating connections).

Ofgem safeguards customers' interests by setting the level of charges we are allowed to recover associated with the output commitments we must deliver. Ofgem is able to make comparisons across all eight gas distribution networks. The output targets are defined such that Cadent Gas maintains safe and reliable networks; make a positive contribution to sustainability and protect the environment; provide connections to supply new consumers and support new gas entry points into the network; meet social obligations such as reducing fuel poverty and raising awareness of the dangers of carbon monoxide; and provide an agreed standard of service to consumers and other stakeholders.

On 9 December, Cadent submitted its final 2021-2026 RIIO-2 Business Plan to Ofgem. This submission followed a period of intense consultation that included over one million interactions with customers and stakeholders. The plan sets out Cadent's ambition to transform the service it delivers for customers, communities and employees.

Our plan for 2021-2026

Keeping the energy flowing safely and reliably	• 99.9% reliability keeping customers on gas • 1,705km of old metallic mains replaced each year • World-class emergency response service with average arrival time of 35 mins • More than £500m cost efficiency savings for customers
A quality experience for all our customers and stakeholders	• Reduction in time interrupted for customers in multi-occupancy buildings • Offering a suite of targeted interventions • Raising awareness of the Priority Services Register through direct conversations, partnerships and colleague training • Raising awareness of the dangers of carbon monoxide across our networks
Tackling climate change and improving the environment	• Target a 14-17% reduction in leakage from our network • Significant step towards carbon neutrality in our operation by 2026 • Innovation to decarbonise the North West with hydrogen • Enabling network capacity for greener resources
Trusted to act for our communities	• More than 1% of post-tax profit invested back into our communities through our charitable foundation - c. £6m p.a • More than 10% saving per annum in customer bills in real terms (excluding inflation) • Simple, clear and comprehensive reporting against all of our customer commitments • 60% of colleagues giving back to our communities through volunteering

Ofgem released their draft determinations in early July with responses required in early September. Ofgem's final determinations are expected to be published in December and we will continue to work closely with them throughout the remainder of the process.

Strategic Report (continued)

For the year ended 31 March 2020

COVID-19 Statement - Supporting our customers and colleagues in a challenging time

In March 2020, at the start of the COVID-19 pandemic, we took immediate steps to implement our business continuity plans ahead of the lockdown announcement by the Government on the 23 March. We quickly adapted and prepared; carrying out specific risk assessments for our essential services, prioritising emergency response and urgent safety issues to keep the gas flowing and the National Gas Emergency Service fully operational. Our critical operations continued with the appropriate policies and Personal Protective Equipment (PPE) and office safeguarding in place.

During the lockdown period, our customer facing iron mains replacement and new connections work were suspended in line with Government guidance. We continued the critical maintenance and repair work needed, whilst making sure we followed Government guidance and taking extra safety precautions when we enter customers' homes, businesses, schools and hospitals.

In April, a full remobilisation plan was developed to enable us to move forward with our work effectively once restrictions eased. In May, we carried out a trial mains replacement project in Doncaster to measure customers' acceptability of our work. This trial was very successful and further trials were carried out in each network during May and early June. As restrictions eased on the 15 June, we have continued to work closely with the HSE and BEIS to ensure that the safety related considerations of restarting our mains replacement work, which involved customer contact has been able to resume at the earliest opportunity.

We continue to follow all necessary guidance whilst working closely with Ofgem, HSE and BEIS to navigate the pandemic and continuously monitor our business continuity plans and working practices to make sure our people stay safe and we keep the energy flowing for our 11 million customers.

Financial impact of COVID-19

The COVID-19 pandemic has had a negligible impact on our income statement, statement of financial position and statement of cash flows for the 2019/20 financial year.

For 2020/21, we expect some continuing impact, driven by additional direct COVID-19 costs for items such as PPE and employee absence for self-isolation and shielding reasons. We also anticipate that the refocussing of our capital programmes, in particular the iron mains replacement programme, will cause a reduction in the volume of work delivered however we are anticipating higher unit costs to deliver this work programme will been seen for some time to come. We are actively engaging with Ofgem regarding the treatment of any affected regulatory output measures linked to COVID-19 and how these will be dealt with in the remaining year of this regulatory period (RIIO-1) and the implications to our RIIO-2 Business Plan submission for output commitments made from April 2021, together with the treatment of costs directly or indirectly incurred as a result.

<u>Shipper income and credit risk</u>

Our transportation income, which represents over 93% of our total revenues is invoiced to shippers based on their agreed capacity with only around 3% of these revenues linked to volume of gas used. This linkage provides a significant insulation from fluctuations in gas demand that have or might result from COVID-19. To the extent that revenues do reduce as a result of lower gas consumption any shortfall will be recoverable through transportation revenues in subsequent years.

We have assessed whether there is any impact of COVID-19 on the recoverability of trade and other receivables. Given the nature of the business our principal commercial exposure relates to shipper income which is governed by Section V of the Gas Transportation Uniform Network Code. There are a number of actions we take to mitigate credit risks including the holding of security in the form of cash, obtaining letters of credit and ensuring major diversionary work is invoiced and paid in advance of the work commencing.

COVID-19 Statement - Supporting our customers and colleagues in a challenging time (continued)

Shipper income and credit risk (continued)
Changes to the Uniform Network Code are required to be agreed across the gas industry with involvement from Ofgem and we have actively engaged with Ofgem to help protect shippers and suppliers by supporting the proposal for the 'COVID-19 Liquidity Relief Scheme'. This will involve the relaxation of network charge payment terms for those suppliers and shippers who are facing cash flow challenges as a result of COVID-19 whilst ensuring that Cadent is not exposed to any credit losses that might emerge should a shipper subsequently fail. We have capped our exposure to the timing of these deferrals to £50m and all deferrals are scheduled to be repaid prior to March 2021. We believe that this is in the best interest of the wider gas supply market whilst ensuring that the transportation sector is insulated from these risks.

Liquidity risk
We have assessed whether there is any impact of COVID-19 on our liquidity risk. Between March and June 2020 Cadent took advantage of the VAT deferral scheme deferring a total of £69m to be paid to HMRC by 31 March 2021. At 31 March 2020, the Group had undrawn credit facilities and cash totalling £988m made up of available Revolving Credit Facilities of £630m, investments in short-term money funds of £332m and cash of £26m. We also retain the capacity to raise additional debt if required from the debt capital markets, the recent interest in the debt transaction completed in March 2020 demonstrates significant demand remains for Cadent Group debt. With no term debt due to mature until September 2021 and the high degree of predictability of our regulated revenue and operating and capital expenditure, we have assessed the liquidity risk as low but we continue to monitor this very closely.

Notwithstanding the high degree of certainty over our cash flows we have assessed a series of sensitivities to cash flow (including to revenues, operating expenditure, capital investment, inflation and interest rates) and believe that the level of cash and undrawn facilities provides adequate protection against reasonably possible downside changes in our assumptions should COVID-19 persist.

Supply chain
We continue to work with our supply chain so that our systems and networks have the necessary materials and parts to allow us to continue to operate our critical activities and maintain the safety of our assets. We have successfully increased procurement of the appropriate PPE to ensure the safety of our employees and their interactions with customers to allow our safety critical work to be completed whilst complying with the relevant guidance. This now also applies to the resumption of our connections and iron mains replacement customer facing work. As a mitigation against the Brexit risk we had already increased our inventory levels of priority materials; these inventory levels will be maintained going forwards as a precaution against COVID-19 and our departure in December from the EU. Our regular engagement with Government and our regulators, as well as following all restrictions regarding management of the spread of COVID-19, is expected to continue for the foreseeable future. We have met supplier liquidity issues with a more flexible payment regime to help sustain those business affected.

COVID-19 Statement - Supporting our customers and colleagues in a challenging time (continued)

Pensions

In light of COVID-19 and the resulting impact on financial markets there is significant uncertainty over certain pension asset valuations, particularly of the property (£273m) and unquoted equities (£730m) portfolios which together represent c.15% of the £6,492m asset value as at 31 March 2020. A higher degree of caution has been attached to the property valuations received from external parties due to the unknown future impact that COVID-19 might have on the real estate market. For the property portfolio, our valuation reports from our surveyors are subject to material valuation uncertainty clauses as set out in the RICS guidance due to the impact COVID-19 has had on previous market evidence, however, we do not believe that this is likely to result in a material change in the value disclosed. For unquoted equities where it was not possible to obtain valuations at 31 March 2020 (£54m of the £730m unquoted equities portfolio) a benchmark reduction based on market evidence has been applied.

Going concern

The Board's consideration of the going concern status of the company is an extension of our annual business planning process. The process includes financial forecasting, a robust risk management assessment, regular budget reviews as well as scenario planning incorporating industry trends, considering any emerging issues and economic conditions. Our business strategy aims to enhance our long-term prospects by making sure our operations and finances are sustainable.

Management have performed analysis of the potential impact of the COVID-19 pandemic on revenue, profit and cash flows. As the vast majority of revenue is set in accordance with the regulatory charging methodology which, being a capacity-based regime, provides relative stability and predictability of cash flows, the overall impact was limited. The analysis included modelling both the base case and a reasonable worst case scenario cash flow forecast that factored in the key impacts of COVID-19 including additional one-off increases in other costs such as cleaning, safety equipment, IT and employee absence, the refocusing of our capital programmes, reduced revenues as a result of lower gas consumption and additional working capital requirements from the shipper relief scheme or from any potential supplier failure. The forecasts were considered against the ability to access existing undrawn facilities alongside its ability to access long-term debt markets (a recent transaction in Cadent Finance Plc in March 2020 was significantly oversubscribed) and short-term cash positioning. Where required, available mitigating actions to maintain liquidity (including for example reducing discretionary costs and deferring expenditure) were considered as part of the assessment. It was concluded that sufficient headroom existed in the forecast and against the requirements of our key banking covenants of net debt to RAV and Interest Cover Ratio. Management therefore concluded that no reasonably possible downside scenario existed wherein Cadent would be unable to continue as a going concern. After due consideration and having concluded there were no material uncertainties, it was recommended to the Board in August 2020 that the financial statements be prepared on the going concern basis.

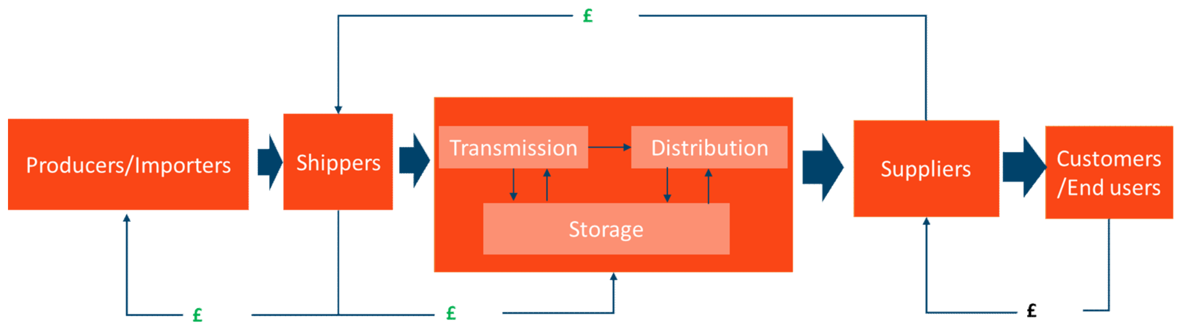
Revenue

Most of our revenue is set in accordance with our regulatory agreements. This is referred to as our 'allowed revenue' and is calculated based on a number of factors. These include:

• investment in network assets;
• operational "run the business" costs (including tax and pensions);
• performance against incentives;
• regulatory return on equity and cost of debt; and
• inflation adjustments.

Our allowed revenue gives us a level of certainty over future revenues if we continue to meet our output commitments as well as the efficiency and innovation targets included in the RIIO-1 price control.

Revenue (continued)
We collect our revenue by levying charges on gas shippers, who will then recover these costs from energy suppliers, who in turn recover these costs through end user energy bills. Quite often, the shipper and supplier organisations are one and the same. The chart below summarises the fund flows.



Other income comprises all activities outside the regulated business principally relating to cash fees paid by customers, typically property owners / developers, for connections fees and typically developers or large infrastructure projects for altering, diverting or relocating part of our existing network.

Cash flow
Our ability to convert revenue to cash is an important factor in the ongoing reinvestment in our business. Securing low-cost funding, carefully managing our cash flows and efficient development of our networks are essential to maintaining strong sustainable returns for our shareholders. Cash generation is underpinned by our charging methodology (part of the industry's network code) which being a capacity based regime provides stability and predictability of cash flows.

Investment
We invest efficiently in our networks to deliver strong regulated asset growth over the long-term. This drives additional future revenues, which in turn generates additional cash flows and allows us to continue reinvesting in our networks and providing sustainable dividends to our ultimate shareholders.

This approach is critical to the sustainability of our business. By challenging our investment decisions, we continue to deliver reliable, cost-effective networks that benefit our customers. The way in which our investment is funded is also an important part of our business. The long-term, sustainable nature of our assets and our credit ratings help us secure efficient funding from a variety of sources.

Strategic Report (continued)

For the year ended 31 March 2020

Consolidated Results

Income Statement

Revenue

Revenue of £2,115m (2019: £1,986m) is driven by our transportation charges (to recover our Regulatory Allowed Revenue) which are levied on gas shippers, who will then recover these costs from energy suppliers, who in turn recover these costs through consumers energy bills. Each year our revenues are largely fixed in line with the profile set out by our price control settlement which determines the pricing of our services to the gas shippers. Any differences between our allowed revenues and the amounts collected through our pricing are adjusted in future periods. Revenues for the year ended 31 March 2020 include higher capacity income driven by inflation and the collection of additional passthrough costs as well as higher connections and diversions income driven by the completion of several significant projects in the year.

Operating profit

Operating profit before exceptional items and remeasurements was £929m (2019: £782m) with operational expenditure largely comprising charges associated with our usage of the National Grid Gas Transmission network, business rates and employment costs of our direct workforce and contract partners. COVID-19 did not have any material impact on operating profit in 2019/20.

Operating profit after exceptional items was £649m (2019: £623m loss). The increase in profit on prior year of £1,272m is due to the additional revenue above, and a lower goodwill impairment charge of £227m (2019: £1,372m).

Exceptional items and remeasurements

Exceptional costs of £280m (2019: £1,405m) were largely driven by a goodwill impairment charged in the year of £227m.

During the year, management completed the annual impairment test required for the goodwill and indefinite life intangibles that it holds on its balance sheet. The impairment test required the comparison of the carrying value of the net assets of the income generating unit (Cadent Gas Limited) and its recoverable amount. The impairment review was completed following receipt of the Ofgem Draft Determinations on 9 July 2020 as management were aware of its potential impact on the recoverable amount. The Draft Determinations included a challenging draft set of outputs, indicating the possibility of a further impairment arising over and above the impairment booked in the prior year following the publication by Ofgem of the RIIO-2 Sector Specific Methodology. Additionally, management considered the potential short- and long-term impacts of COVID-19 and have incorporated any risks identified into the impairment test. This calculation indicated that the recoverable amount was lower than the carrying amount and an impairment charge of £227m (2019: £1,372m) was recognised.

As part of our drive to transform the business, we have also incurred exceptional transformation costs this year. Restructuring costs totalling £34m have been recognised, of which £25m relates to a voluntary redundancy programme announced in May 2019 (severance payments of £7m and additional pension liabilities of £18m). As we pushed to complete the separation of our IT systems from National Grid, we incurred exceptional costs of £17m associated with this work (2019: £15m).

Remeasurements of £14m have been recognised within finance costs in relation to the remeasurement of derivatives. This is due to changes in the mark-to-market values of index-linked swaps, which have been affected by inflation and interest rate assumptions.

Net finance costs
Net finance costs before remeasurements of £263m (2019: £248m) were driven by interest on external debt funding. There were net £14m (2019: £13m) remeasurement costs arising from the changes in fair value of derivative financial instruments during the year.

Taxation
Our effective rate of corporation tax for the year, before exceptional items and remeasurements, is 19.2% (2019: 18.4%). After exceptional items and remeasurements the effective rate increases to 88.2% (2019: (10.2%)) due to an exceptional deferred tax charge of £213m in the year (2019: £Nil) following the change to the UK corporation tax rate, plus the goodwill impairment charged to exceptional items which is non-deductible.

In common with other utilities, we have a significant deferred tax provision that mainly relates to the benefits received in the past from tax allowances on capital expenditure before the depreciation on those assets has been charged to our profits. This provision is released to the income statement as the depreciation catches up with the tax allowances received. The provision is calculated at the rate of tax applicable when the provision is expected to reverse. Since the Government had previously legislated that the UK corporation tax rate would reduce to 17% from 1 April 2020, deferred tax had therefore been provided on that basis at 31 March 2019. Budget 2020 however introduced further legislation to increase the UK corporation tax rate to 19% from 1 April 2020 and the charge of £213m in the year reflects the restatement of the tax rate at which we now expect the provision to reverse.

During the year and in accordance with our obligations under Finance Act 2016 Schedule 19, we published our Tax Strategy statement (which can be found on the Corporate governance pages of cadentgas.com). We are committed to being a responsible and compliant taxpayer and the Tax Strategy statement sets out our approach to a number of key tax policies including our approach to tax governance and risk management, our attitude towards tax planning, our risk appetite in relation to UK taxation and our approach to dealing with HMRC.

Statement of Financial Position
The consolidated statement of financial position sets out all the Group's assets and liabilities at the period end. It is dominated by the value of our physical assets and the corresponding borrowings that fund our capital investment programmes.

Capital Investment
Capital investment was £856m (2019: £736m) and is primarily associated with the ongoing gas mains replacement programme which saw 1,809km of mostly cast iron pipes replaced by polyethylene pipe during the year. Increased investment from the previous year was driven by the ramping up of our major capital works programmes including the HS2 diversions activity.

Cash flow and net debt
Borrowings (both current and non-current) at 31 March 2020 were £9,905 million (2019: £9,542 million) mainly comprised fixed rate and index-linked debt.

Driven by the need to fund our capital investment programme, the Group has a material amount of debt, with regular maturities and requirements for new incremental debt, therefore the Group operates a pro-active policy of meeting credit investors and the Group's relationship banks regularly to provide updates and information to facilitate ongoing access to the capital markets.

Cash flow and net debt (continued)

In readiness for RIIO-2 we have worked to improve the resilience of our debt portfolio; ensuring that our financing strategy was focused on securing the required debt in advance of our needs in order to reduce any financing risk. In the year we successfully refinanced the Group's outstanding loan facilities extending the maturity to 2024 (previously 2021 and 2022). This included repaying the existing syndicated term loans of £393m and £218m and drawing new syndicated term loans of £300m and £220m. The Revolving Credit Facilities at Cadent Gas Limited (£500m) and Quadgas MidCo Limited (£200m) were replaced with new facilities with maturity dates of 2024. We also issued a 16-year fixed rate bond of £300m under the £6bn Euro Medium Term Note programme and repaid £400m of the £650m 2021 maturity notes issued in 2016 under a Tender offer. In March we were pleased to issue the UK's first transition bond – a 12-year EUR 500m bond - to invest in the retrofit of gas distribution network assets, principally the iron mains replacement programme. The bond was very positively received by investors and was oversubscribed by a factor of 8 times. Cadent Gas Limited will use the proceeds of the bond to replace pipeline to facilitate in the future to carry low-carbon gases and reduce methane leakage.

The Group continues to have at its disposal sufficient undrawn, committed borrowing facilities at competitive rates for the medium term.

As at 31 March 2020, Quadgas MidCo Limited was rated BBB+ (stable outlook) by S&P, with any notes issued by the company rated BBB (stable outlook).

Uses and sources of cash

The vast majority of our revenues are set in accordance with the regulatory charging methodology (part of the industry network code) which, being a capacity-based regime, provides relative stability and predictability of cash flows. Our ability to convert revenue to profit and cash is important and by managing our operations efficiently and safely we are able to generate sustainable operating cash flows. Net cash inflow from operations in 2019/20 was £1,078m, £45m higher than in 2018/19, primarily due to increases in our regulated revenues and the cost reductions achieved through our transformation programme[1].

Investing efficiently in the development of our network is essential to maintaining strong performance for our customers and long-term sustainable returns for our shareholders.

Liquidity

We maintain liquidity headroom to ensure that the Group can meet all financial obligations and to fund operations, even during periods of market disruption and times of uncertainty. We manage liquidity by requiring at least 12 months' liquidity available at all times, with at least two months' liquidity available within 24 hours.

As at 31 March 2020, liquidity was provided by a combination of immediately available cash and committed bank facilities. The cash held in Money Market Funds was £358m, following receipt of the debt proceeds issued in the latter part of the year. All funds held with the Money Market Funds can be drawn with no notice. We also have access to Revolving Credit Facilities from our relationship banking group. This allows for drawings of up to £700m, with a balance of £70m drawn at 31 March 2020.

[1] A presentational adjustment has been made to reclassify £80m of cash flows from capital contributions from investing activities to operating activities in 2019/20. The comparative value of £91m has also been restated in the consolidated statement of cash flows. See note 1(s) of the financial statements for further information.

Liquidity (continued)

We also maintain Bond programmes through Cadent Finance Plc and Quadgas Finance Plc, subsidiaries of the Group, which allows efficient access to debt capital markets, in a range of different currencies. The combination of short-term liquid funds and access to longer term borrowings allows us to keep a healthy level of liquidity which has become increasingly important in the wake of COVID-19.

Intangible assets

Goodwill of £1,713m (2019: £1,940m) has decreased due to an impairment charge of £227m during the year which was recognised within exceptional items in the income statement. Under the requirements of IAS 36, this impairment was allocated to the goodwill balance of the cash generating unit (the business of gas distribution at the total Cadent business group level - the level at which the performance of Cadent business group is managed and at which key decisions are currently made regarding resources) and an impairment loss of £227m (2019: £1,372m) was recognised against the goodwill balance. The impairment review was completed following receipt of the Ofgem Draft Determinations on 9 July 2020 as management were aware of its potential impact on the recoverable amount. The Draft Determinations included a challenging draft set of outputs, indicating the possibility of a further impairment arising over and above the impairment booked in the prior year following the publication by Ofgem of the RIIO-2 Sector Specific Methodology. Additionally, management considered the potential short and long-term impacts of COVID-19 and have incorporated any risks identified into the impairment test.

The Group also holds a balance of £2,143m (2019: £2,143m) relating to the gas distribution licence and £90m relation to software (2019: £63m).

Pensions

The Group operates pension arrangements for employees many of whom are members of Section C of the defined benefits section of the National Grid UK Pension Scheme (NGUKPS) which is closed to new entrants. Membership of the defined contribution scheme is offered to all new employees.

With respect to the Defined Benefit pension arrangements the Group made contributions of £72m during the course of the year including £40m as part of a deficit reduction plan agreed with the Trustees.

On an IAS 19 basis the defined benefits pension scheme is in a net asset position of £917m at 31 March 2020 (2019: net asset position of £690m) due to actuarial gains and favourable financing assumptions. In light of COVID-19 there was some uncertainty over certain asset valuations of our property and unquoted equities portfolio as at 31 March 2020 however updated valuations were obtained in June 2020 which supported only a minimal decrease to the asset valuations.

Pensions (continued)

One of the remaining steps following the sale of National Grid's remaining stake in the Group in June 2019 is the creation of a new pension scheme into which existing members of the Section C of NGUKPS will be transferred, on a like for like basis, during the financial year 2020/21. A new corporate Trustee company was incorporated on 19 December 2019, 'Cadent Gas Pension Trustee Limited' as well as two holding companies 'Cadent Gas Pension Property Company 1 Limited' and 'Cadent Gas Pension Property Company 2 Limited' incorporated on 25 March 2020 and a further holding company 'Cadent Gas Pension Services Limited' incorporated on 17 June 2020.

Impact of new accounting standards – IFRS 16

IFRS 16 'Leases' is applicable to reporting periods beginning on or after 1 January 2019, and has therefore been adopted by the Group for the year commencing 1 April 2019.

In line with the assessment disclosed in the Group's Annual Report and Financial Statements for the year ended 31 March 2019, the adoption of IFRS 16 'Leases' resulted in the recognition of £26m right-of-use assets (principally relating to contractual arrangements the Group had for land and buildings, motor vehicles and plant and machinery) and £23m lease liabilities (after adjustments for prepayments recognised as at 31 March 2019). On transition, overall net assets increased by £2m and net current liabilities were £6m higher due to the presentation of a portion of the liability as a current liability. In addition to this, the Group continued to recognise lease liabilities and assets of £6m relating to pre-existing finance lease liabilities recognised under IAS 17 as at 31 March 2019.

Profit after tax has decreased by £2m for the year ended 31 March 2020 as a result of adopting the new standard.

Operating cash flows have increased and financing cash flows decreased by £6m as repayment of the principal portion of the lease liabilities is classified as cash flows from financing activities.

The Group's activities as a lessor are not material and hence this has not had a significant impact on the financial statements.

Performance summary

We believe that transparent disclosure of performance against our targets is essential. The KPIs reported are reviewed regularly by the Cadent Gas Limited Executive Committee and the Safety, Health, Environment and Security (SHES) Committee, who are accountable for environmental policy and performance. Some of our measures have been imposed by our regulator and are marked accordingly.

Risk and Compliance Process Overview

The Board is committed to protecting and developing our reputation and business interests. It has overall responsibility for risk management within the business. It has set the risk appetite for the Group and reviews the risk profile at least annually.

We have adopted a risk management model which places responsibility for actively managing risks firmly with the business. There is a central team who set the risk management framework, facilitate reporting, provide advice and challenge to the business.

Risk and Compliance Process Overview (continued)

Executive Committee members regularly review their risks to assess their current status, progress of mitigation plans and to identify emerging or developing risks. The Executive Committee reviews the Group's risk profile on a regular basis bringing together top down and bottom up risk management. In line with our value of curiosity, we are always seeking better ways to deliver our risk management process. The Audit and Risk Committee reviews the effectiveness of the overall risk management policy and process on an annual basis.

We have adopted the internationally recognised 'Three Lines of Defence Model' in order to assure the Executive, Audit and Risk Committee and Board that risks have been identified and are being suitably managed. In addition to the risk management process there are several further second line assurance processes operated by specialist teams embedded within the business. These teams provide assurance over the effectiveness of the financial and non-financial internal controls operating across the business. Our in-house Internal Audit Team are supported by specialist co-source providers to form the Third Line of Defence. An independent reporting line directly to the Audit and Risk Committee to ensure that the Internal Audit Team can provide an expert, independent and objective opinion on the current state of controls to the Audit and Risk Committee.

The Board discharges its responsibility for monitoring the effectiveness of the risk management process and internal controls through the Audit & Risk Committee's annual review and regular assurance reports. This includes compliance with our license conditions which is recognised as part of our 'failure to comply with legal and regulatory requirements or failure to deliver regulatory outputs' principal risk.

Climate change risk management

We support and are committed to implementing the recommendations of the Task Force on Climate Related Financial Disclosures (TCFD). The processes we use to identify, assess and manage risks are embedded in the business and have been used to address the Climate Change risk. Our risk management processes are outlined below.

Financial risk management

The management of the Group and the execution of the Group's strategy are subject to a number of financial risks. The Directors have identified the need to manage the Group's material financial risks, including liquidity, credit, interest rate and market risks including foreign currency risks together with pandemics, as a result of the emerging COVID-19 issues in March. These risks are monitored through a Group Treasury management function ("Treasury") which invests surplus funds, mitigates foreign exchange exposure and manages borrowings for Quadgas MidCo Limited and its subsidiaries.

Treasury also seeks to limit third party counterparty risk which arises from the investment of surplus funds and the use of derivative financial instruments. Treasury monitors the exposure that the Group has with any one counterparty against agreed limits and these limits are monitored regularly and updated for changes in credit ratings.

Liquidity risk

Liquidity risk is the risk that the Group will not have sufficient funds to meet the obligations or commitments resulting from its business operations or associated with its financial instruments, as they fall due. The Group manages the liquidity profile of its assets, liabilities and commitments so that cash flows are appropriately balanced, and all funding obligations are met when due. This is achieved through maintaining a prudent level of liquid assets and arranging funding facilities.

Financial Risk Management (continued)

Liquidity risk (continued)

As at 31 March 2020 the COVID-19 pandemic prompted a thorough review with regard to required levels of liquidity. The Group initiated additional analysis to assess existing facilities and align liquidity levels with possible COVID-19 scenarios. This analysis concluded that the significant financial resources available to the Group are sufficient, no additional liquidity has been sought. Monitoring of the situation is ongoing. See page 4 for further detail.

The Board is responsible for monitoring the policies, setting the limits on the maturity of liquidity and deposit funding balances and taking any action as appropriate.

Credit risk

The Group takes on exposure to credit risk, which is the risk that financial loss arises from the failure of a customer or counterparty to meet its obligations under a contract as they fall due. Credit risk arises principally from trade finance and treasury activities. The Group has dedicated standards, policies and procedures to control and monitor credit risk. The counterparties under treasury activities consist of financial institutions. In accordance with IFRS 9, the Directors have considered and quantified the exposure of the Group to counterparty credit risk and do not consider there to be a material credit risk adjustment required. The exposure to counterparty credit risk will continue to be monitored. Although the Group is potentially exposed to credit loss in the event of non-performance by counterparties, such credit risk is controlled through regular credit rating reviews of the counterparties and by limiting the total amount of exposure to any one party. Management does not anticipate any counterparty will fail to meet its obligations.

Significant changes in the economy or in the utilities sector could result in losses not necessarily provided for at the statement of financial position date. There are only 40 principal Shippers (customers) that we trade with. The creditworthiness of each of these is closely monitored. Whilst the loss of one of the principal customers (e.g. default of a gas shipper) could have a significant impact on the business in terms of disruption to revenue recovery, the exposure to such credit losses would be mitigated in most cases by the protection given by the Uniform Network Code (the industry governance contract). The Code requires customers to provide security for their transportation services, requires them to pay monthly and links to a supplier of last resort process which ensures a defaulting shipper’s customers are reallocated to another shipper who picks up forward liabilities. Nonetheless, the credit management process must be closely adhered to, to avoid such circumstances, and the business’s management therefore closely monitors credit risk and adherence to this process.

Market risk

Market risk is the risk that future cash flows of a financial instrument, or the fair value of a financial instrument, will fluctuate because of changes in market prices. Market prices include foreign exchange rates, interest rates, inflation, equity and commodity prices. The main types of market risk to which the Group is exposed are interest rate risk, inflation risk and exchange risk in relation to debt issued in foreign currency. The Board is required to review and approve policies for managing these risks on an annual basis. The Board approves all new hedging instruments entered into. The management of market risk is undertaken by reference to risk limits, approved by the Chief Financial Officer or Director of Treasury for Cadent Gas Limited, under delegated authority from the Board.

Financial Risk Management (continued)

Market risk (continued)
The Group has no significant transactional foreign exchange, equity or commodity exposure. The Group has exposure to interest rate risk and inflation risk and this is explained in the sections below. The Group borrows in the major global debt markets at fixed, index-linked and floating rates of interest, using derivatives, where appropriate, to generate the desired effective interest basis.

The company has limited direct exposure to the impacts of Brexit, however we recognise the potential macroeconomic impacts which are addressed through our financial risk management.

We will continue to monitor the progress of trade negotiations and the potential impacts to our business of a new trade deal with the EU or a no deal outcome. The main short-term risk that we face is potential supply chain disruptions. We continue to engage with our suppliers to understand their Brexit plans and are closely monitoring their delivery performance. We have also taken a prudent approach and increased our stock levels to preserve the delivery of operational activities. Other risks will continue to be reviewed as more information becomes available regarding the final outcome and the impact that it could have for us in the long-term, but analysis carried out to date did not reveal a wider material risk in relation to Brexit for our business. Although the risk remains subject to monitoring, the overall potential risk to the business is considered to be low and has therefore not been included as a principal risk.

The emerging potential risks of COVID-19 are also being monitored through our crisis management framework under executive supervision. A detailed risk assessment is in place and continues to be updated as the situation evolves to ensure that we consider and manage health and operational safety risks in line with Government advice.

Interest rate risk
Interest rate risk is the risk that either future cash flows of a financial instrument, or the fair value of a financial instrument, will fluctuate because of changes in market interest rates. The Group's floating rate borrowings and derivatives are exposed to a risk of change in cash flows due to changes in interest rates. The Group's fixed rate borrowings and derivatives are exposed to a risk of change in their fair value due to changes in interest rates.

Our principal risks and uncertainties include:

1. Failure to protect consumers' interests
We must keep both current, and future consumers, safe and warm whilst delivering good value for money. Although a small proportion of the overall bill, we are mindful of the effect that network costs have on our consumers' energy bills and are committed to improving the service levels they can expect from us. This is a key feature of our RIIO2 business plan which we submitted in December 2019.

Strategic Report (continued)
For the year ended 31 March 2020

1. Failure to protect consumers' interests (continued)

Risk Management:
• Customer performance is recognised as a priority for our business. We have engaged customers extensively and worked closely with our Customer Engagement Group to ensure that customer interests are at the heart of RIIO2 business plan.
• We are pioneering developments in a cross industry safeguarding customers group looking at services that are provided to customers in vulnerable situations.
• We continue to invest in our networks to maintain and improve service levels.
• We have a culture of continuous improvement to drive down cost and better serve our customers.
• We have established clear customer targets which are closely monitored, with improvement plans in place where necessary. This is monitored and governed by our Customer Performance Committee.
• There is a commitment, at all levels of the organisation, to improve customer performance. This is reinforced through regular employee communications, which share good practice across the organisation.
• Special measures in place for customers identified by the Priority Services Register and mechanisms in place to help customers register as priority customers.

2. Health, safety and environment
Safety will always be a top priority and whilst major incidents are rare, human factors, asset and system malfunctions carry an inherent risk of harm to those who work for us and the communities we serve. We are also mindful of the impact that our operations could have on the environment in which we work, and take care to ensure that we manage our environmental risks to minimise these potential impacts. In order to ensure we continue to keep the energy flowing it is imperative that we secure our people and assets so that we can maintain the essential service that our customers rely on. A major incident could cause disruption for our customers and loss of credibility with our regulators. It could also result in damage to our reputation and regulatory enforcement including significant financial penalties or claims.

Risk management:
• We have robust safety and ISO14001 accredited environmental management systems in place which are underpinned by a Health & Safety Executive accepted safety case.
• There is visible leadership and commitment to health, safety and environmental matters, including regular leadership safety visits which has created a strong safety culture throughout the organisation.
• We operate process safety controls which are supported by robust incident investigation and review processes.
• We have long-term, risk based investment and replacement programmes to ensure that we maintain a safe and efficient network.
• Our dedicated Security and Property teams monitor developing security threats, provide visible deterrents at our keys sites and ensure that appropriate personal security advice is provided to colleagues.
• In the event of an incident we have well practiced crisis management response procedures in place.
• To support continual improvement across the industry there are structures in place for cross-industry sharing of good practice and learning.

3. Climate change and changes in operating landscape

Climate change is a substantial existential risk and opportunity for many organisations which plays out in 3 ways:

Firstly, given the nature of our infrastructure and the essential services that we provide, we have a unique opportunity to help drive forward the UK's hydrogen economy to decarbonise our heat and transport systems which will be essential for the UK to deliver its stretching climate change targets and meet the changing expectations of consumers and society.

Secondly, we are also aware of our own potential to contribute to climate change and are actively seeking ways to reduce this.

Thirdly, our own operations may be impacted by the effects of climate change – for example the effects of more severe winters and flood events may put strain on our operating model.

As a regulated business, our future opportunities are directly affected by factors driving the landscape of the energy industry. These include emergent technologies, political events, changes in consumer habits and social trends, media coverage, public opinion and Government views, which are reflected in the decisions of policy makers and regulators to define the way in which we can run our business.

Risk management:

• We have a unique role to play in the de-carbonisation of the UK's heat and transport systems. Our 'Future Role of Gas' programme looks at future scenarios and how we can support the delivery of the UK's hydrogen economy.

• This year we have pioneered innovation projects to demonstrate the viability of hydrogen networks through large scale demonstration projects such as HyDeploy and HyNet.

• By working with partners to connect more sustainable sources of gas, such as biomethane, we are already providing consumers with access to more sustainable energy.

• We are also taking steps to reduce our own carbon footprint through our mains replacement and use of gas powered HGV vehicles.

• We monitor external developments to understand potential disruptive forces, including emerging technologies, changes in societal norms and the political consensus which may affect our business plan to ensure that we proactively plan for and respond to them.

• We will maintain credibility for delivery through the careful management of our current regulatory obligations and workload.

• We undertake regional and national stakeholder engagement to understand policy, customer drivers and the regulatory landscape.

• There are extensive programmes in place through the Energy Networks Association, Energy Innovation Centre and with BEIS, Ofgem and third parties to share innovations with other gas distribution networks and across utilities and third parties to ensure we are implementing best practice and coordinating our approach to solving decarbonisation.

4. Failure to effectively manage assets and maintain network reliability
To ensure that we efficiently maintain a safe and reliable network for our customers, we must implement an effective asset management framework. It must, through appropriate policies and procedures, good quality asset data, suitable investment and competent personnel, deliver an effective process for preserving the integrity of both individual assets and the operation of our networks as a whole to deliver the right service to our customers and stakeholders.

Failure to effectively manage risk on individual assets or on our networks could lead to asset failures which may result in customer service failures, a safety or environmental incident or failure to meet our regulatory standards of service. This could also damage our reputation and may lead to additional costs, enforcement action or financial penalties.

Risk management:
• We have an asset management framework in place that is independently accredited to ISO55001 standard.
• We have engineering and asset management teams in place to manage the framework and ensure good quality asset decisions and investments are made.
• The framework is supported by decision support tools to aid complex decision making and ensure resilience is maintained.
• Engineering policies and procedures are in place to ensure that assets are appropriately operated and maintained.
• A replacement programme is in place and agreed with our regulators to ensure that ageing assets are replaced.
• In the event of asset failure, insurance is in place to compensate for damage arising.
• In the event of an incident we have well-practiced crisis management response procedures in place.
• Our RIIO2 business plan submission has set out investment cases to justify continued investment in our network to ensure that customer standards of service are maintained going forwards.

5. Failure to secure critical skills and engagement
The people who work for us are essential to the success of our business. Both our direct workforce and those engaged through our partners and supply chain must be resilient and capable of adapting to the needs of the industry. The ageing profile of our workforce and competition for limited skilled resources in means this is a key risk that we must manage. In operating an emergency service, we rely on stocks and supplies being available when they are most needed, if they were not this would significantly impact the service that we are able to provide to our customers.

Risk management:
• To build our internal resource pool and develop our future pipeline of talent, we have developed a series of talent and training programmes, including those for graduates and apprentices.
• To attract and retain the right people, our reward packages are competitively benchmarked and incentivise performance aligned to the performance of the company's objectives.
• To ensure that employees remain engaged we undertake regular monitoring of employee engagement which allows us to identify and address any areas of concern.
• Strategic workforce planning helps us understand our future resourcing needs, including those operationally critical roles to evaluate the best mitigation strategies.
• Succession plans are in place for operationally critical roles.
• As this is an industry wide issue we also support development of the STEM subjects through associated bodies such as the ENA.
• We work closely with our Strategic Partners to monitor the availability of skilled teams to undertake our mains replacement work and have targeted recruitment programmes.

5. Failure to secure critical skills and engagement (continued)

• Our dedicated Supply Chain Team work closely with our partners and suppliers to identify critical supplies and closely monitor and manage stock levels throughout the year to ensure critical supplies are maintained.

• We monitor and work closely with our strategic partners to ensure delivery of key projects and programmes with suitable escalation routes and governance in place for risks and issues to be identified and resolved.

6. Cyber breach or critical system failure

Due to the nature of our business, we rely on technological systems to support our operational delivery. We recognise that our critical national infrastructure (CNI) systems may be a potential target for cyber threats. We must protect our business assets, personal data and infrastructure and be prepared for a malicious attack. To ensure that we efficiently maintain a safe and reliable network for our customers, we implement an effective IS asset management framework. It must, through appropriate policies and procedures, good quality asset data, suitable investment and competent personnel, preserve the integrity of both individual assets and the operation of our networks as a whole.

Risk management:

• Critical processes and systems are understood and security controls designed on a risk based approach.

• Cyber controls are operated by the dedicated Cadent Cyber operations team. Our approach to cyber and information security is governed by our Information Security Framework.

• We use industry best practices as part of our cyber security policies, processes and technologies. Our cyber security programme is a global programme of work which started in 2010 and continues to be modified and updated to this day. This programme is intended to reduce the risk that a cyber threat could adversely affect the Group's business resilience.

• We continually invest in cyber strategies that are commensurate with the changing nature of the security landscape. This includes collaborative working with Business, Energy and Industrial Strategy (BEIS) and the Centre for Protection of National Infrastructure on key cyber risks and development of an enhanced CNI security strategy.

• Business Continuity Management (BCM) and resilience steering Groups are in place to ensure the effective management of BCM and resilience across our business.

• BCM plans are in place for critical processes and routinely tested.

• Our Digital Risk and Security team have been engaging with the appropriate agencies to ensure we have appropriate controls in place to manage our obligations under the Network Information Security Regulations which all providers of critical national infrastructure must comply with.

7. Failure to comply with legal and regulatory requirements or failure to deliver regulatory outputs

We set high standards of ethics and compliance that we expect those working for us to follow. As a regulated business, compliance with legislative and regulatory requirements is fundamental to our ability to operate. Failure to comply with legal and regulatory requirements could result in disruption to the operational business, penalties and damage our reputation. Failure to deliver regulatory outputs would fall short of our own expectations and indicate unacceptable failures in delivering an adequate service to our customers. It could also damage our credibility with the regulator and customers and impact our ability to earn future returns.

Risk management:

• We have structured our business around the delivery of our regulatory outputs. Dedicated operational teams are in place to focus on the delivery of our standards of service, delivery of our mains replacement programme and upgrading our network assets.

• Detailed outputs were set at the beginning of the RIIO price control and these are carefully monitored through a governance framework which includes weekly issues calls and monthly customer performance reviews to ensure that emerging risks and issues are escalated and managed in a timely manner.

7. Failure to comply with legal and regulatory requirements or failure to deliver regulatory outputs (continued)

• There is a strong compliance culture. This is reflected in our values of 'courage' and 'commitment'. To sustain this culture, all employees are trained in our ethical guide, 'Always Doing the Right Thing' and suppliers are expected to sign up to our supplier code of conduct. This is also supported by a strong 'tone from the top' and internal communication programme.

• We operate a compliance process which includes the review of our compliance with legal and regulatory obligations and is reported through the organisation to our Audit and Risk Committee and Board.

• We have a horizon scanning forum to identify, and ensure we prepare, for regulatory changes and developments.

8. Pandemic risk

A pandemic outbreak is an externally driven, long-term cyclical risk, with human history featuring irregular but periodic pandemic outbreaks. Whilst all pandemics are by their nature very serious, some are devastating. The likelihood of a pandemic occurring is understood to be increasing due to the loss of biodiversity and increasing anti-microbial resistance, which is a subset of this wider risk. The immediate impact of an outbreak is also generally increasing due to the inter-connectivity of the modern world. However, society ability to respond to outbreaks is ever improving in terms of action to limits a pandemic's spread; advances in medical responses and technological innovation which provide a route by which activities can continue, in a modified form, during a pandemic outbreak.

The impact of a pandemic risk is highly dependent on the nature and attributes of the specific pathogen but include:

• Operational impacts – non-availability of people both colleagues and in the supply chain, due to illness, caring responsibilities or medically advised restrictions;

• Macroeconomic impacts – significant uncertainly and an actual reduction in output impacting inflation, the cost of debt and the stability of suppliers.

The actions to prepare and respond to these potential impacts include both actions specific to a pandemic but arising from considering how a pandemic impacts other risks.

Due to the essential nature of our core services and care for our customers and colleagues as well as those we come into contact with, Cadent has to be prepared for pandemic outbreaks. The mitigation of this risk is partly an internal activity, but also relies to a substantial degree on interactions across a range of stakeholders in a number of sectors.

This risk has crystalised in the current COVID-19 outbreak which is specifically addressed in our COVID-19 statement on page 3.

Risk management:

• An external threat scanning process to alert us to any developing widespread health issues.

• Internal sickness absence and occupational health processes.

• Up to date, relevant and periodically tested business continuity plans, with a focus on the continuance of essential services.

• A dedicated Health team that both supports and advises directly and has the ability to call upon external support where required.

• A crisis management framework with rapidly implementable 'Gold, Silver and Bronze' governance. Supported by a wide range of two directional communication channels to support colleagues both as individuals and coworkers.

8. Pandemic risk (continued)

• Deep and wide experience within the leadership team of incident and crisis response including experience of a pandemic outbreak exercise.

• A comprehensive and well-understood risk assessment and risk management process that takes account of uncertainty in available information and can adapt and respond well to situational changes.

• Strong links to stakeholders including those within Government, Ofgem and the HSE.

• Structured and collaborative arrangements with Trade Unions.

• Financial structuring that can adapt to short-term ‘shocks’ in the wider economic environment and regulatory support to sustain the business during prolonged impact.

• Immediate scenario modelling, particularly in relation to workforce planning and liquidity, to gauge key actions.

• The ability of the non-operational teams to rapidly reprioritise workload and respond to rapid changes in operational requirements for example homeworking.

S172 Statement

The following statement describes how the Directors have had regard to the matters set out in section 172(1) (a) to (f) when performing their duty under section 172 of the Companies Act 2006.

The company has no operational activities and no employees, it is a financing company for bank debt and privately held subsidiary level debt. The company’s main purpose is to remove the increased administrative burden and level of legal compliance required of a public company within the Group. As a wholly owned subsidiary holding company within the Cadent Gas Group (“the Group”), the Directors consider the impact of the company’s activities on its shareholder, its subsidiaries and other stakeholders. For detail on how the Directors have had regard for the interests of the employees of the Group, see the employees section within Directors report on page 23.

The company’s stakeholders are consulted routinely on a wide range of matters including funding decisions, investment strategy, delivery of the Group’s strategy, governance and compliance with Group policies and financing matters in relation to the company’s investments, with the aim of maximising investment returns for the benefit of its shareholder and ensuring that the company maintains high standards of business conduct and governance.

As an investment vehicle for the Group, the company obtains and provides finance to fellow subsidiary companies via intercompany balances. The Board considers the company’s investments in light of the Group’s corporate and social responsibility strategy, as such the Board receives information on these topics from management to make better informed Board decisions.

The Directors continued to provide oversight governance of its subsidiaries to ensure that they comply with the Group’s policies and maintain high standards of business conduct. The company provides regular updates on its activities to the Directors. During the year under review three new Directors were appointed to broaden the skills and experience of the Board.

For further information on the Group activities and disclosure please refer to the Cadent Gas Annual Report and Accounts 2019/20. Whilst not directly regulated itself, the company maintains a close relationship with the Ofgem (The Office of Gas and Electricity Markets), via the indirect subsidiary company Cadent Gas Limited.

The Strategic Report was approved by the Board and signed on its behalf by:

M W Braithwaite
Director
12 August 2020

Quadgas MidCo Limited

Directors' Report

For the year ended 31 March 2020

The Directors present their Report and the audited financial statements of the Group and the company for the year ended 31 March 2020.

Principal activities and business review

A full description of the Group's and company's principal activities, businesses, key performance indicators and principal risks and uncertainties is contained in the Strategic Report on pages 1 to 20, which are incorporated by reference into this report.

Directors

The Directors of the company during the year and up to the date of signing of the financial statements were:

M W Braithwaite
J Korpancova
H C Higgins
D Karnik
P D Noble
D J Xie
A M Al-Ansari
N J Axam
H Su
M W Mathieson
R Greenleaf
E B Fidler
S Fennell (Appointed 15 May 2019)
J Bao (Appointed 28 June 2019)
HNM De Run (Appointed 6 April 2020)
M J Gregory (Resigned 15 May 2019)
I M Coucher (Resigned 24 March 2020)

Future developments

Details of future developments have been included within the Strategic Report on page 1.

Dividends

Our dividend policy is to balance the distribution of available surplus funds to shareholders but after having the forward committed cash requirements of the business to support our investment programmes and importantly the managing the appropriate level of gearing. During the year we paid dividends totalling £275 million (2019: £340 million).

Political donations and political expenditure

The Group did not make any political donations or political expenditure during the current year (2019: £Nil).

Research and development

Expenditure on research and development for the Group was £7 million during the current year (2019: £6 million).

Directors' indemnity

Quadgas HoldCo Limited (an indirect parent company) has arranged, in accordance with the Companies Act 2006 and the Articles of Association, qualifying third party indemnities against financial exposure that Directors may incur in the course of their professional duties. Alongside these indemnities, Quadgas HoldCo Limited places Directors' and Officers' liability insurance for each Director.

Going concern
The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 1 to 20. The financial position of the company, its cash flows, liquidity position and borrowing facilities are described in this Strategic Report on pages 1 to 20. In addition, note 28 to the financial statements include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk. The company has considerable financial resources together with long-term contracts with a number of customers and suppliers across different geographic areas. As a consequence, the Directors believe that the company is well placed to manage its business risks successfully despite the current uncertain economic outlook and challenging RIIO-2 framework.

Having made enquiries and reviewed management's assessment of going concern including the uncertainties posed by COVID-19 on our cash flows and the subsequent impact on headroom against available facilities, the Directors consider it appropriate to prepare the financial statements on a going concern basis. The going concern basis presumes that the company has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements are signed. Further detail is provided in the going concern section of the COVID-19 analysis included on page 5.

Capital structure
The capital structure of the Group consists of shareholders' equity, as disclosed in the consolidated statement of changes in equity, and net debt.

Control and Risk Management
The Group has established internal control and risk management systems in relation to the process for preparing consolidated financial statements. The key features of these internal control and risk management systems are:

• The risk assurance function and management conducts various checks on internal financial controls periodically.

• Management regularly monitors and considers developments in accounting regulations and best practice in financial reporting, and where appropriate, reflects developments in the consolidated financial statements. Appropriate briefings and/or training are provided to key finance personnel on relevant developments in accounting and financial reporting. The Audit and Risk Committee is also kept appraised of such developments.

• The financial statements are subject to review by the Financial Reporting function for unusual items, unexplained trends and completeness. Any unexplained items are investigated.

• The Financial Reporting function compares the financial statements to the management accounts received during the year and obtains explanations for any material differences.

• The Group's consolidation, which consolidates the results of each business unit and makes appropriate adjustments, is subject to various levels of review by the Financial Reporting function.

• The Audit and Risk Committee for the Quadgas HoldCo Group and the Board review the draft consolidated financial statements. The Audit and Risk Committee receives reports from management and the external auditor on significant judgements, changes in accounting policies, changes in accounting estimates and other pertinent matters relating to the consolidated financial statements.

Post balance sheet events
There are no post balance sheet events.

Disclosure of information to auditor
Having made the requisite enquiries, so far as the Directors in office at the date of the approval of this report are aware, there is no relevant audit information of which the auditor is unaware and each Director has taken all reasonable steps to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

Auditor
A resolution to re-appoint Deloitte LLP as auditor of the company will be proposed at the Annual General Meeting for shareholder approval.

Employees
Across the Group, we communicate with our employees across a wide variety of topics and have established effective channels to do this, for example: emails, the Group intranet, cascade briefings, sms alerts, voice messages and in-house newsletters. We believe that it is important to seek the views of our employees to inform decision making on matters which may affect them, and both formal and informal mechanisms are used to ensure that regular consultation takes place with employees and their trade union representatives.

We are committed to equality, inclusion and diversity and aim to support employees in achieving and maintaining a good balance between their work and personal lives. We promote equality in the development and application of our policies, through our recruitment processes and in training and development opportunities.

It is our policy that people with disabilities are treated fairly in relation to job applications and opportunities for training, career development and promotion. When employees are unable to continue working in their current role due to disability during their employment, every effort is taken to make reasonable adjustments, provide suitable training and identify alternative roles, if required.

Read about our policies in relation to ethical conduct, gender pay, anti-corruption and bribery, modern slavery and other topics at https://cadentgas.com/about-us/corporate-governance.

Environmental Policy
We are committed to delivering high standards of environmental performance, protecting and enhancing the environment, and seeking new, innovative and sustainable ways to lighten our environmental footprint and create long-term value for our customers, our people and stakeholders.

Our environmental ambition is underpinned by three primary commitments:
- Reduce the impact of climate change by implementing mitigation and adaptation measures.
- Ensure environmental sustainability is considered in our decision making and inspire our people to consider it in everything they do.
- Improve our environmental management system to protect the environment and reduce the risk of environmental incidents.

Directors' Report (continued)

For the year ended 31 March 2020

Environmental Policy (continued)

We strive to innovate in our day-to-day operations, continuously improving and finding new ways to deliver the highest standards of environmental performance, embedding it as part of our everyday activities and decision making, whether in the office or in the field.

We are committed to leading on sustainable gas usage and have identified wider use of the renewable compressed natural gas as transport or heating fuel as a route to delivering a low carbon future. We are also at the forefront of developing and understanding the role that hydrogen will play as a low or zero-emission fuel for the future.

The table below quantifies the Groups business carbon footprint in tonnes of CO2 equivalent :

GHG emissions and energy use data for period 1 April 2019 to 31 March 2020

Scope 1 and 2 (Direct emissions)	**Current reporting year 2019-2020**	**Comparison reporting year 2018-2019**
Gas usage from buildings /tCO_2e Scope 1	1,044.00	811.13
Natural gas shrinkage (Leakage + Theft of Gas + Own use of gas)/tCO_2e Scope 1	1,632,973.70	1,694,053.20
Fuel usage from commercial vehicles, company cars and greyfleet /tCO_2e Scope 1	19,841.00	20,077.00
Purchased electricity for own use /tCO_2e Scope 2	7,318.80	8,992.00
Total Scope 1 and 2 /tCO_2e	1,661,177.50	1,723,933.33
Scope 1 and 2 energy consumption /kWh As above	2,452,504,563.14	2,257,911,041.03
Intensity metric: Total scope 1 and 2 tCO_2e per £m turnover	785.43	864.13
Intensity metric: Total scope 1 and 2 tCO_2e per km of our gas network	12.68	13.16
Scope 3 (Indirect emissions)		
Business travel /tCO_2e Rail, Air, Ferry, Car Hire	278.00	1,574.23
Emissions from production and delivery of purchased PE pipe /tCO_2e	20,039.00	12,897.00
Contractor vehicles /tCO_2e Mains Replacement contractor fuel use	17,648.56	15,653.00
Total Scope 3 emissions /tCO_2e As above	37,965.56	30,124.23
Total annual net emissions /tCO_2e Scope 1 (including shrinkage and leakage, 2, 3 emissions	1,699,143.06	1,754,057.56
Intensity metric: Total emissions /tCO_2e per £m turnover	803.38	879.23
Intensity metric: Total emissions /tCO_2e per km of network length	12.97	13.39
Intensity metric: Total emissions /tCO_2e per GWh throughput	6.24	6.82

Methodology

Methodology: Data provided here is in line with annual Business Carbon Footprint reporting to OFGEM using DEFRA conversion factors. Conversion factors are updated annually. Additional lines such as contractor vehicles have been added here for full disclosure and in line with annual returns to OFGEM. Where market-based factors are stated these are provided annually by our electricity suppliers. Total annual net emissions figure uses location based methodology. Intensity metrics have been discussed via the Energy Networks Association (ENA).

For more information please see the Groups Safety and Sustainability report within the Cadent Gas Limited Annual Report and Accounts 2019/20.

Quadgas MidCo Limited

Directors' Report (continued)

For the year ended 31 March 2020

Statement of Directors' responsibilities

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Generally Accepted Accounting Practice, including FRS 101 'Reduced Disclosure Framework' ('FRS 101')). 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 company and of the profit or loss of the Group and company for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union have been followed for the Group financial statements and United Kingdom Accounting Standards, including FRS 101, have been followed for the company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and company and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

The Directors are also responsible for safeguarding the assets of the Group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors' Report was approved by the Board and signed on its behalf by:

M W Braithwaite
Director
12 August 2020

Registered office:
Ashbrook Court, Prologis Park, Central Boulevard, Coventry, CV7 8PE

Registered in England and Wales
Company registration number: 10615396

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF QUADGAS MIDCO LIMITED

Report on the audit of the financial statements

1. Opinion

In our opinion:

- the financial statements of Quadgas MidCo Ltd (the 'parent company') and its subsidiaries (the 'Group') give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 March 2020 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the consolidated income statement;
- the consolidated statement of comprehensive income;
- the consolidated and parent company statements of financial position;
- the consolidated and parent company statements of changes in equity;
- the consolidated statement of cashflows;
- the related notes 1 to 34 to the consolidated financial statements; and
- the related notes 1 to 16 to the parent company financial statements.

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

2. 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 the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (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.

3. Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: • Valuation of goodwill; • Valuation of pension and other post-retirement benefit assets; and • Judgement over the classification of non-GDSP expenditure as capital or operational.
Materiality	The materiality that we used for the Group financial statements was £38.9 million which was determined on the basis of adjusted profit before tax.
Scoping	Audit work to respond to the risks of material misstatement was performed directly by the audit engagement team.
Significant changes in our approach	Our approach is largely consistent with the prior year, however, we have considered the impact of COVID-19 within the business.

4. Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where: • the Directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or • the Directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Group's or the parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.	We have nothing to report in respect of these matters.

5. Key audit matters

Key audit matters are those matters that, in our professional judgement, 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 forming our opinion thereon, and we do not provide a separate opinion on these matters.

5.1. Valuation of goodwill and indefinite life intangibles

Key audit matter description	The book value of goodwill and indefinite life intangibles as at 31 March 2020 is £3,856 million (2019: £4,083 million) and represents the amounts recognised on acquisition of 100% share capital of Cadent Gas Limited, including its subsidiary, Cadent Finance Plc, and 100% of share capital of Cadent Services Limited on 31 March 2017, less cumulative impairments. As part of the purchase price allocation, goodwill of £3,312 million was recognised together with an intangible asset for the gas distribution licence of £2,143 million. An impairment loss of £1,372 million was recognized against the goodwill balance at 31 March 2019. A further impairment loss of £227 million was recognized against the goodwill balance at 31 March 2020. These assets are required to be assessed annually for impairment. The impairment assessment involves management judgement in considering whether the carrying value of these assets is recoverable. The key assumptions and judgements underpinning the impairment reviews are:-

	- discount rate; - inflation rate; - regulatory weighted average cost of capital ("WACC"); and - RAV exit multiple. These assumptions are sensitive to the guidance published by Ofgem for the next price control period (RIIO-GD2) which is due to commence from 1 April 2021. The price controls are still undergoing consultation and therefore are currently uncertain. Further details on the key sources of estimation uncertainty underpinning indefinite life assets can be found in note 2 and note 12, and in the strategic report on pages 7 and 10. Details on the sensitivity of the above impairment reviews to changes in key assumptions are disclosed in note 29.
How the scope of our audit responded to the key audit matter	We, together with our valuations experts, have: • Obtained an understanding of relevant controls around the calculation of the business' value in use, and the review of discount rate, inflation forecasts (CPIH), regulatory WACC, where most sensitivity lies on the cost of equity, and the RAV exit multiple; • understood and challenged each of management's key assumptions for the RIIO2 price control period and beyond, together with management's sensitivity analysis; • We have considered and assessed the impact of COVID-19 pandemic on the future cash flows; • reviewed the appropriateness of the discount rate, forecast inflation, regulatory WACC and RAV exit multiple; • evaluated the consistency of management's assumptions within the impairment model with those applied in the Group's forecast and going concern models; • evaluated management's business plan, including their forecast cashflows; • assessed the implied RAV multiple against other comparable regulated businesses; • completed a detailed arithmetical review of management's model for inconsistencies and errors; and • reviewed the disclosures included in the financial statements.
Key observations	Based on the work performed we concluded that the key assumptions used to determine the recoverable amount of the goodwill and indefinite life intangible assets are appropriate.

5.2. Valuation of pension and other post-retirement benefit assets

Key audit matter description	The net retirement benefit asset of £917 million includes assets totalling £6,492 million of which £730 million (11%) are unquoted equities. The COVID-19 pandemic has resulted in the valuation of certain property assets and unquoted equities (including private equities and alternative funds) being subject to increased estimation uncertainty. Given the range of estimation uncertainty we identified a key audit matter associated with the valuation of the unquoted equities. Further details are included within critical accounting estimates and judgements note in note 2 and pensions note 27 to the financial statements, and in the strategic report on page 5. Details on the sensitivity of the unquoted equities are disclosed in note 29.

How the scope of our audit responded to the key audit matter	We, together with our pension valuations experts, have performed the following procedures in response to the key audit matter: • Obtained an understanding of relevant controls over the valuation of unquoted pension assets; • agreed asset values to external valuation reports provided by fund managers; and • assessed the reasonableness of the valuation methodologies applied especially for those unquoted equities where it was not possible to obtain valuations at 31 March 2020. This included reviewing publicly available information on these assets, comparing the valuations to internal benchmarks and confirmation of inputs used by management to determine asset values;
Key observations	Based on the work performed we conclude that the valuation of unquoted equities within pension assets is appropriate.

5.3. Judgement over classification of non-GDSP expenditure as capital or operational

Key audit matter description	The Group invests heavily in fixed assets and more specifically in the infrastructure and gas network annually, ranging from major replacement projects to minor repairs and maintenance works. During the year the Group has invested £841 million in capital expenditure. There is a risk that expenditure which is operating in nature is capitalised into fixed assets due to incorrect identification and mapping of activities. This may lead to the overstatement of fixed assets and operating profit. We identified that there is increased risk in relation to costs associated with non-GDSP (Gas Distribution Strategic Partners). As the classification of such capital expenditure and operating expenditure directly affects the Group's financial performance, we identified a key audit matter relating to the overstatement of non-GDSP capital expenditure and we determined that there was a potential for fraud through manipulation of this balance. Further details are included within note 13.
How the scope of our audit responded to the key audit matter	We have performed the following procedures in response to the key audit matter: • obtained an understanding of relevant controls related to the recognition of capital expenditure; • challenged management's judgement and their policies relating to the classification of capital expenditure, operating expenditure and infrastructure maintenance expenditure where a high level of management judgement is involved; • performed an analytical review of the expenditure capitalised and expensed during the year; • tested a sample of capital projects by inspecting supporting documentation from subcontractors regarding the works completed and assessed whether such works were capitalised or expensed appropriately; • We have considered and assessed the impact of COVID-19 lockdown on the ongoing capital projects to ascertain that costs not directly associated with the capital projects are not capitalised; • for internal payroll costs capitalised, on sample basis, inspected the timesheets and chargeable rates for employees and ascertained that the employees worked on capital projects; and • completed a reconciliation between the fixed assets register and the general ledger.

Key observations	Based on our audit procedures we consider the classification of expenditure as capital to be appropriate.

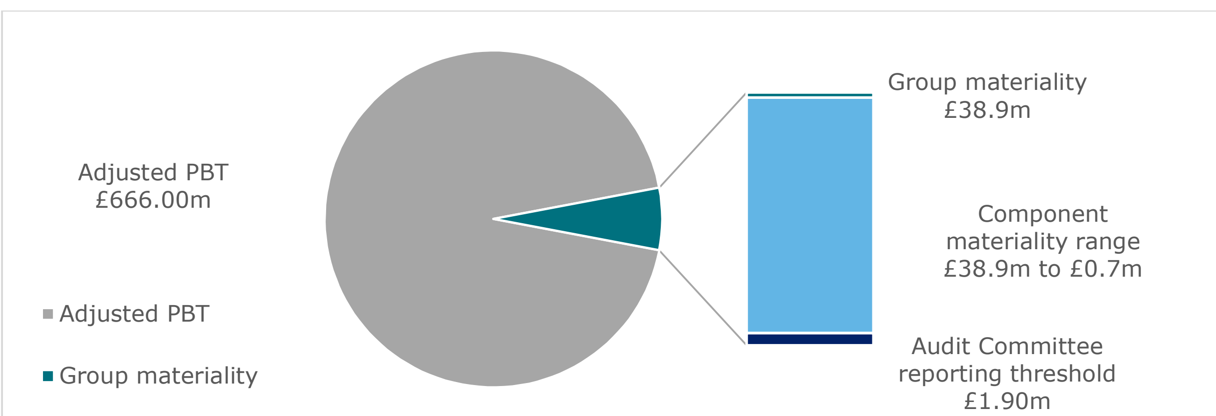
6. Our application of materiality

6.1. Materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Materiality	£38.9 million (2019: £36.4 million)	£27.2 million (2019: £25.2 million)
Basis for determining materiality	Approximately 6% of adjusted pre-tax profit (i.e. Profit before tax, exceptional items and remeasurement)	Parent company materiality equates to 0.4% of total assets, which is capped at 70% of Group materiality
Rationale for the benchmark applied	Pre-tax profit adjusted for exceptional items and certain remeasurements was considered to be the most relevant benchmark as it is of most interest to stakeholders. Furthermore, exceptional items and certain re-measurements are volatile and materially impact the Group's performance each year due to events and transactions that are not part of the underlying activities of the Group, and excluding them enables a more consistent basis with which to consider the Group's performance on an ongoing basis.	The entity acts as an intermediate holding and acquisition company with intercompany borrowings. Hence, total assets has been selected as the appropriate benchmark for calculation of materiality.



6.2. Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. Group performance materiality was set at 70% of Group materiality for the 2020 audit (2019: 70%). In determining performance materiality, we considered factors including our understanding of internal controls across a number of areas of the audit, management's willingness to make process improvements as well as to correct errors identified and the stability of the finance team. We considered the lack of prior history of material misstatements in the previous audit and the lack of factors resulting in a disproportionate number of significant and higher risks of material misstatement.

6.3. Error reporting threshold

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £1.9 million (2019: £1.8 million), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

7. An overview of the scope of our audit

7.1. Identification and scoping of components

The Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material misstatement at a Group level. All companies in the Group were subject to full statutory audits.

The Group comprises five statutory companies. These were subject to full statutory audits using component materialities ranging from £709,000 to £38.9 million (2019: £709,000 to £36.2 million).

All audit work was performed by the Group audit team.

At the Group level, we also tested the consolidation process.

8. Other information

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

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

In connection with our audit of the financial statements, 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 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 or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in respect of these matters.

9. Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement, 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's and the 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.

10. 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.

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

Report on other legal and regulatory requirements

11. 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 the Directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Group and the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the Directors' report.

12. Matters on which we are required to report by exception

12.1. Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- 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.

We have nothing to report in respect of these matters.

12.2. Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of Directors' remuneration have not been made.

We have nothing to report in respect of this matter.

13. 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.

Jacqueline Holden FCA (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom
12 August 2020

Quadgas MidCo Limited

Consolidated income statement

For the year ended 31 March 2020

	Notes	**2020 £m**	**2020 £m**	2019 £m	2019 £m
Revenue	4		**2,115**		1,986
Operating costs	5		**(1,186)**		(1,204)
Operating profit/(loss)					
Before exceptional items	5	**929**		782	
Exceptional items	6	**(280)**		(1,405)	
Total operating profit/(loss)	5		**649**		(623)
Finance income	9		**18**		16
Finance costs					
Before exceptional items and remeasurements	9	**(281)**		(264)	
Exceptional items and remeasurements	6/9	**(14)**		(13)	
Total interest payable and similar charges			**(295)**		(277)
Profit/(loss) before tax					
Before exceptional items and remeasurements		**666**		534	
Exceptional items and remeasurements	6	**(294)**		(1,418)	
Total profit/(loss) before tax			**372**		(884)
Tax					
Before exceptional items and remeasurements	10	**(128)**		(98)	
Exceptional items and remeasurements	10	**(200)**		8	
Total tax			**(328)**		(90)
Profit/(loss) after tax					
Before exceptional items and remeasurements		**538**		436	
Exceptional items and remeasurements		**(494)**		(1,410)	
Profit/(loss) for the year			**44**		(974)

The results reported above relate to continuing activities.

The notes on pages 39 to 106 are an integral part of the financial statements.

Quadgas MidCo Limited

Consolidated statement of comprehensive income

For the year ended 31 March 2020

	Notes	**2020 £m**	2019 £m
Profit/(loss) for the year		**44**	(974)
Other comprehensive income:			
Items that will not be reclassified to profit or loss			
Remeasurements of post-employment benefit obligations	27	**176**	132
Tax on remeasurements of post-employment benefit obligations	10	**(33)**	(23)
Tax arising as a result of the reversal of the expected reduction in the UK tax rate	10	**(13)**	-
Total items that will never be reclassified to profit or loss		**130**	109
Items that may be reclassified subsequently to profit or loss			
Net losses in respect of cash flow hedges		**(17)**	(4)
Net losses in respect of cost of hedging reserve		**(4)**	(8)
Amortisation of cost of hedging reserve		**5**	5
Tax on net losses in respect of cash flow hedges	10	**3**	1
Total items that may be reclassified subsequently to profit or loss		**(13)**	(6)
Other comprehensive income for the year, net of tax		**117**	103
Total comprehensive income/(loss) for the year		**161**	(871)

The notes on pages 39 to 106 are an integral part of the financial statements.

The results reported above relate to continuing activities.

Quadgas MidCo Limited

Consolidated statement of financial position

As at 31 March 2020

	Notes	**2020 £m**	2019 £m
Non-current assets			
Intangible assets	12	**3,946**	4,146
Property, plant and equipment	13	**11,444**	10,977
Pension and other post-retirement benefit assets	27	**917**	690
Trade and other receivables	16	**21**	44
Derivative financial assets	17	**44**	8
Total non-current assets		**16,372**	15,865
Current assets			
Inventories	15	**10**	10
Trade and other receivables	16	**240**	219
Current asset investments	18	**332**	339
Cash and cash equivalents		**26**	12
Total current assets		**608**	580
Total assets		**16,980**	16,445
Current liabilities			
Trade and other payables	19	**(594)**	(560)
Borrowings[1]	21	**(139)**	(66)
Lease liabilities[1]	22	**(9)**	-
Current tax liabilities		**-**	(56)
Provisions	23	**(16)**	(15)
Total current liabilities		**(758)**	(697)
Non-current liabilities			
Derivative financial liabilities	17	**(73)**	(38)
Borrowings[1]	21	**(9,766)**	(9,476)
Lease liabilities[1]	22	**(18)**	-
Deferred tax liabilities	10	**(2,179)**	(1,928)
Provisions	23	**(87)**	(80)
Accruals and deferred income	20	**(12)**	(27)
Total non-current liabilities		**(12,135)**	(11,549)
Total liabilities		**(12,893)**	(12,246)
Net assets		**4,087**	4,199
Equity			
Share capital	24	**1**	1
Cash flow hedge reserve		**(6)**	8
Cost of hedging reserve		**-**	(1)
Retained earnings		**4,092**	4,191
Total equity		**4,087**	4,199

[1]Borrowings in the comparative period include finance leases, as accounted for under IAS 17. In the current period these liabilities have instead been recorded as part of lease liabilities, as required by IFRS. See note 1 (c) for further details.

The notes on pages 39 to 106 are an integral part of the financial statements.

The consolidated financial statements on pages 34 to 106 were authorised and approved for issue by the Board of Directors on 12 August 2020 and were signed on its behalf by:

M W Braithwaite
Director
Quadgas MidCo Limited
Company registration number: 10615396

Quadgas MidCo Limited

Consolidated statement of changes in equity

For the year ended 31 March 2020

	Share capital £m	Share premium account £m	Cash flow hedge reserve £m	Cost of hedging Reserve £m	Retained earnings £m	Total £m
At 1 April 2019	**1**	**-**	**8**	**(1)**	**4,191**	**4,199**
Changes due to adoption of IFRS 16	**-**	**-**	**-**	**-**	**2**	**2**
Balance at 1 April 2019 (restated)	**1**	**-**	**8**	**(1)**	**4,193**	**4,201**
Profit for the year	**-**	**-**	**-**	**-**	**44**	**44**
Other comprehensive income/(loss) excluding amortisation of cost of hedging reserve	**-**	**-**	**(14)**	**(4)**	**130**	**112**
Amortisation of cost of hedging reserve	**-**	**-**	**-**	**5**	**-**	**5**
Total comprehensive income/(loss) for the year	**-**	**-**	**(14)**	**1**	**174**	**161**
Equity dividends (note 11)	**-**	**-**	**-**	**-**	**(275)**	**(275)**
At 31 March 2020	**1**	**-**	**(6)**	**-**	**4,092**	**4,087**

	Share capital £m	Share premium account £m	Cash flow hedge reserve £m	Cost of hedging reserve £m	Retained earnings £m	Total £m
At 1 April 2018	1	-	12	1	5,396	5,410
Loss for the year	-	-	-	-	(974)	(974)
Other comprehensive income/(loss) excluding amortisation of cost of hedging reserve	-	-	(4)	(7)	109	98
Amortisation of cost of hedging reserve	-	-	-	5	-	5
Total comprehensive income/(loss) for the year	-	-	(4)	(2)	(865)	(871)
Equity dividends (note 11)	-	-	-	-	(340)	(340)
At 31 March 2019	1	-	8	(1)	4,191	4,199

The cash flow hedge reserve in relation to the cross-currency interest rate swap contracts will be recycled to the income statement over the life of the hedged items.

The notes on pages 39 to 106 are an integral part of the financial statements.

Quadgas MidCo Limited

Consolidated statement of cash flows

For the year ended 31 March 2020

	2020	2019
		(Restated[1])
	£m	£m
Cash flows from operating activities		
Total operating profit/(loss)	**649**	(623)
Adjustments for:		
Exceptional items	**280**	1,405
Depreciation, amortisation and impairment	**390**	369
Increase in inventories	**-**	(4)
Decrease in trade and other receivables	**2**	9
Increase in trade and other payables	**33**	13
Capital contribution income	**(106)**	(55)
Changes in provisions	**9**	-
Gain on disposal of property, plant and equipment	**(2)**	(1)
Changes in pensions and other post-retirement obligations	**(55)**	(53)
Capital contributions received [1]	**80**	91
Cash flows relating to exceptional items	**(26)**	(14)
Cash generated from operations	**1,254**	1,137
Tax paid	**(176)**	(104)
Net cash inflow from operating activities	**1,078**	1,033
Cash flows from investing activities		
Purchases of intangible assets	**(36)**	(22)
Purchases of property, plant and equipment	**(819)**	(645)
Disposals of property, plant and equipment	**1**	2
Interest received	**1**	1
Net decrease/(increase) in financial investments	**7**	(178)
Net cash flow used in investing activities	**(846)**	(842)
Cash flows from financing activities		
Proceeds received from loans	**1,313**	1,391
Repayment of loans	**(1,015)**	(1,046)
Repayment of lease liabilities (2019 - repayments under finance leases)	**(7)**	(1)
Interest paid	**(233)**	(207)
Dividends paid to shareholders	**(275)**	(340)
Net cash flow used in financing activities	**(217)**	(203)
Net increase/(decrease) in cash and cash equivalents	**15**	(12)
Net cash and cash equivalents at the start of the period	**3**	15
Net cash and cash equivalents at the end of the period	**18**	3
Comprising:		
Cash	**26**	12
Overdraft	**(8)**	(9)
	18	3

[1]A presentational adjustment has been made to reclassify cash flows from capital contributions from investing activities to operating activities. See Note 1(s) for further detail.

1 Summary of significant accounting policies

Quadgas MidCo Limited is a private company limited by shares and is incorporated and domiciled in the United Kingdom and is registered in England and Wales. The address of its registered office is Ashbrook Court, Prologis Park, Central Boulevard, Coventry, CV7 8PE.

The principal accounting policies applied in the preparation of these consolidated financial statements are set out as below. These policies have been consistently applied to the current period presented, unless otherwise stated.

(a) Basis of preparation

The financial statements for the Group have been prepared on the going concern basis under the historical cost convention modified to include certain items at fair value.

As at the date of approving these financial statements, the impact of COVID-19 on the Group's operations are continually being monitored and subject to rapid change. The Directors have assessed the impact by modelling both a base case and a reasonable worst case scenario. As the vast majority of revenue is set in accordance with the regulatory charging methodology which, being a capacity-based regime, provides relative stability and predictability of cash flows, the impact was limited. The reasonable worst case scenario includes:

- one-off increases in other costs such as cleaning, safety equipment, IT and employee absence
- the refocusing of our capital programmes, in particular the iron mains replacement programme, causing a reduction in the volume of work delivered but with higher unit costs to deliver this work programme
- reduced revenues as a result of lower gas consumption
- additional working capital requirements from the shipper relief scheme or from any potential supplier failure

Having considered the reasonable worst case scenario (more detail can be found on page 5), the Group continues to have headroom against the Group committed facilities disclosed in note 21.

In addition, the ability to raise new financing was considered in light of the recent transaction in Cadent Finance Plc in March 2020 where the order book was well in excess of the amount required and it was concluded that the Group has the ability to continue to have access to the debt capital markets if needed.

Based on the above, the Directors have concluded that the Group is well placed to manage its financing and other business risks satisfactorily and have a reasonable expectation that the Group will have adequate resources to continue in operation for at least 12 months from the signing date of these consolidated financial statements. The Director's therefore consider, having concluded that there are no material uncertainties, that it was appropriate to adopt the going concern basis of accounting in preparing the financial statements.

Items included in the financial statements are measured using the currency of the primary economic environment in which the company operates (the 'functional currency'). The financial statements are presented in pounds sterling which is also the company's functional currency.

The consolidated financial statements of Quadgas MidCo Limited have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS), IFRIC interpretations issues and effective and ratified by the European Union as at 31 March 2020 and the Companies Act 2006.

(b) Basis of consolidation

The consolidated financial statements include the results of Quadgas MidCo Limited and its subsidiaries and associate undertakings. Results are included from the date of acquisition or incorporation and excluded from the date of disposal.

Subsidiaries are consolidated where the Group has the power to control a subsidiary.

Associates are accounted for on an equity basis where the Group holding is 20% or more and the Group has the power to exercise significant influence.

1 Summary of significant accounting policies (continued)

(b) Basis of consolidation (continued)

Acquisitions are accounted for using the acquisition method, where the purchase price is allocated to the identifiable assets acquired and liabilities assumed on a fair value basis and the remainder recognised as goodwill.

During 2019/20, Cadent Gas entered into an agreement with the Charities Trust to contribute 1.25% of profit after tax into a Donor Advised Fund (“DAF”). After consideration, we have concluded that the DAF is not controlled by Cadent as the Charities Trust have the power to overrule decisions that do not align with the objectives of the Foundation and the requirements of IFRS 10 have not been met in respect of (1) rights to variable returns and (2) its ability to affect the amount of investor returns. Therefore this has not been consolidated as part of the Quadgas MidCo Limited Group.

(c) New IFRS accounting standards and interpretations

The Group adopted IFRS 16 ‘Leases’ from 1 April 2019. In accordance with the transition provisions in the standard, the Group has applied the simplified transition approach and has not restated comparative amounts for the year prior to first adoption.

IFRS 16 introduces new or amended requirements with respect to lease accounting. It introduces significant changes to lessee accounting by removing the distinction between operating and finance lease and requiring the recognition of a right-of-use asset and a lease liability at commencement for all leases, except for short-term leases and leases of low value assets when such recognition exemptions are adopted.

The Group leases offices, operational buildings, land, equipment and vehicles. Rental contracts typically range from 6 months to 10 years, however land leases can be significantly longer.

Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes.

Prior to the financial year beginning 1 April 2019, leases were classified as either finance leases or operating leases under IAS 17, see note 22 for details. From 1 April 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group, except where certain exemptions apply (as described below).

Applying IFRS 16 for all leases (except as noted below), the Group:

a) Recognises right-of-use assets and lease liabilities in the consolidated statement of financial position, initially measured at the present value of the future lease payments, with the right-of-use asset adjusted by the amount of any prepaid or accrued lease payments in accordance with IFRS 16.

b) Recognises depreciation of right-of-use assets and interest on lease liabilities in the consolidated statement of profit or loss;

c) Separates the total amount of cash paid into a principal portion (presented within financing activities) and interest (presented within financing activities) in the consolidated statement of cash flows.

Under IFRS 16, right-of-use assets are tested for impairment in accordance with IAS 36.

For short-term leases (with a lease term of 12 months or less) and leases of low-value assets (deemed less than £3,500) the Group has opted to recognise a lease expense on a straight-line basis as permitted by IFRS 16.

1 Summary of significant accounting policies (continued)

(c) New IFRS accounting standards and interpretations (continued)

Practical expedients applied

In applying IFRS 16 for the first time, the Group has used the following practical expedients permitted by the standard:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics;
- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review- there were no onerous contracts as at 1 April 2019;
- accounting for operating leases with a remaining lease term of less than 12 months as at 1 April 2019 as short-term leases;
- excluding initial direct costs for the measurement of the right-of-use asset at the date of initial application, and
- using hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

Measurement

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payment that are based on an index or a rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable by the Group under residual value guarantees;
- the exercise price of a purchase option if the Group is reasonably certain to exercise that option;
- payments of penalties for terminating the lease, if the lease term reflects the Group exercising that option; and
- lease payments to be made under reasonably certain extension options.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases in the Group, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the right-of-use asset in a similar economic environment with similar terms, security and conditions.

To determine the incremental borrowing rate, the Group uses recent third-party financing received by the individual lessee of a term similar to that of the lease contract. The weighted average lessee's incremental borrowing rate applied to the lease liabilities on 1 April 2019 was 1.60%.

The lease liability is presented as a separate line in the consolidated statement of financial position, split between current and non-current liabilities.

The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the carrying amount to reflect the lease payments made.

1 Summary of significant accounting policies (continued)

(c) New IFRS accounting standards and interpretations (continued)

The Group remeasures the lease liability (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- the lease term has changed or there is a significant event or change in circumstances resulting in a change in the assessment of exercise of a purchase option, in which case the lease liability is remeasured by discounting the revised lease payments using a revised discount rate.
- the lease payments change due to changes in an index or rate or a change in expected payment under a guaranteed residual value, in which cases the lease liability is remeasured by discounting the revised lease payments using an unchanged discount rate (unless the lease payments change is due to a change in a floating interest rate, in which case a revised discount rate is used).
- a lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured based on the lease term of the modified lease by discounting the revised lease payments using a revised discount rate at the effective date of the modification.

Variable lease payments

Some leases contain variable payment terms. These include:

- Leases for equipment which contain fixed value increases over the life of the lease e.g. final balloon payments. These are included in the lease liability as the amounts are known;
- A gas storage facility for which the rental payments are linked to RPI, and potential future increases in lease payments are not included in the lease liability until they take effect. When adjustments to lease payments based on an index or rate take effect, the lease liability is reassessed and adjusted against the right-of-use asset; and
- Leased equipment where the lease payments are variable as they are based on usage. These costs are not included in the lease liability in line with IFRS 16 because the payments do not meet the definition of a liability until the use occurs. Instead these are recognised in the profit and loss account as and when the expense is incurred.

The table below presents a reconciliation from operating lease commitments disclosed at 31 March 2019 to lease liabilities recognised at 1 April 2019.

	£ m
Operating lease commitments disclosed under IAS 17 at 31 March 2019	27
Effect of discounting the above amounts	(4)
Add: Finance lease liabilities recognised under IAS 17 at 31 March 2019	6
(Less): short-term leases recognised on a straight-line basis as an expense	(1)
(Less): low value leases not recognised as a liability	-
Add: option to purchase payments and embedded leases	1
Lease liability recognised as at 1 April 2019	**29**
Of which are:	
Current lease liabilities	7
Non-current lease liabilities	22
	29

1 Summary of significant accounting policies (continued)

(c) New IFRS accounting standards and interpretations (continued)

Right of use assets
Right-of-use assets are measured at the amount of the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the consolidated statement of financial position. The right-of-use assets are presented within property, plant and equipment in the consolidated statement of financial position. See details in note 13 'Property, Plant and Equipment'.

Right-of-use assets are depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. If the Group is reasonably certain to exercise a purchase option, the right-of-use asset is depreciated over the underlying asset's useful life.

Impact on lessor accounting
The Group does not undertake significant activities as a lessor and did not need to make any adjustments as a result of the adoption of IFRS 16 on its lessor accounting.

Finance leases under IAS 17
For leases previously classified as finance leases the entity recognised the carrying amount of the lease asset and lease liability immediately before transition as the carrying amount of the right of-use-asset and the lease liability at the date of initial application. The measurement principles of IFRS 16 are only applied after that date.

Financial impact of the application of IFRS 16
Profit after tax has decreased by £2m for the year ended 31 March 2020 as a result of adopting the new standard.

The adoption of IFRS 16 'Leases' resulted in the recognition of £26m right-of-use assets and £23m lease liabilities (after adjustments for prepayments recognised as at 31 March 2019). On transition, overall net assets increased by £2m and net current liabilities were £6m higher due to the presentation of a portion of the liability as a current liability. In addition to this, the Group continued to recognise lease liabilities and assets of £6m relating to pre-existing finance lease liabilities recognised under IAS 17 as at 31 March 2019.

Operating cash flows have increased and financing cash flows decreased by approximately £6m as repayment of the principal portion of the lease liabilities is classified as cash flows from financing activities.

1 Summary of significant accounting policies (continued)

(c) New IFRS accounting standards and interpretations (continued)

In line with the standard, short-term leases (less than 12 months) and low value leases (less than £3,500) will continue to be recognised on a straight-line basis as an expense in profit or loss. The amount of short-term leases for the year ended 31 March 2020 is £2m and low value leases is £0.1m.

In summary, the following adjustments were made to the amounts recognised in the statement of financial position at the date of initial application (1 April 2019):

	IAS 17 carrying amount 31 March 2019 £m	Adjustments to recognise right of use assets and lease liabilities £m	IFRS 16 carrying amount 1 April 2019 £m
Property, plant and equipment	10,977	26	11,003
Lease liabilities < 1 year*	-	(7)	(7)
Lease liabilities > 1 year*	-	(22)	(22)
Borrowings < 1 year*	(66)	1	(65)
Borrowings > 1 year*	(9,476)	5	(9,471)
Trade and other receivables	219	(1)	218
Retained earnings	4,191	2	4,193

*Pre-existing finance leases at 31 March 2019 are included within borrowings under IAS 17.

Other

In the current year, the Group has applied a number of amendments to IFRS Standards and Interpretations issued by the IASB that are effective for an annual period that begins on or after 1 January 2019. Their adoption has not had any material impact on the disclosures or on the amounts reported in these financial statements. These are:

- Amendments to IFRS 9 *Prepayment features with negative compensation;*
- Amendments to IAS 28 *Long-term interests in Associated and Joint Ventures;*
- *Annual Improvements to IFRS Standards 2015–2017 Cycle Amendments to IFRS 3* Business Combinations*, IFRS 11* Joint arrangements*, IAS 12* Income Taxes and *IAS 23* Borrowing Costs;
- Amendments to IAS 19 *Employee Benefits Plan Amendment, Curtailment or Settlement; and*
- *IFRIC 23 Uncertainty over Income Tax Treatment.*

At the date of authorisation of these financial statements, the Group has not applied the following new and revised IFRS Standards that have been issued but are not yet effective:

- IFRS 17 *Insurance contracts**;
- Amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture;*
- Amendment to IFRS 7, IFRS 9 and IAS 9 - *Interest rate benchmark reform;*
- Amendments to References to the Conceptual Framework in IFRS Standards;
- Amendments to IFRS 3 *Business Combinations - definition of a business**;
- Amendments to IAS 1 and IAS 8 - *definition of material; and*
- Amendment to IAS 1 - *classification of liabilities*.*

*Denotes that the standard or interpretation has not yet been adopted by the EU (European Union).

The Directors do not expect that the adoption of the Standards listed above will have a material impact on the financial statements of the Group in future periods, except as noted on the next page.

1 Summary of significant accounting policies (continued)

(c) New IFRS accounting standards and interpretations (continued)

Amendment to IFRS 7, IFRS 9 and IAS 9 - Interest rate benchmark reform (phase 1)
Following the financial crisis, the reform and replacement of benchmark interest rates such as GBP LIBOR and other interbank offered rates ('IBORs') has become a priority for global regulators. There is currently uncertainty around the timing and precise nature of these changes. The IASB has embarked on a two-phase project to consider what, if any, reliefs to give from the effects of IBOR reform. For Phase 1, the IASB has issued amendments to IFRS 9, IAS 39 and IFRS 7 that provide temporary relief from applying specific hedge accounting requirements to hedging relationships directly affected by IBOR reform.

Our current portfolio of derivatives consist of those in a designated hedge relationship (cross-currency interest rate swaps) and those not designated in a hedge relationship (our RPI swaps). The cross-currency interest rate swaps and underlying hedged items designated in hedge relationships all pay/receive fixed rates of interest, so no impact is anticipated in this context.

Financial instruments held currently by the Group that directly reference IBOR are term debt, liquidity facilities and RPI swaps. The volume of supplier contracts that reference IBOR are minimal.

The valuation of our derivatives will be impacted on IBOR transition, owing to changes in the market convention of arriving at a discounted fair value.

It is currently expected that SONIA (Sterling Overnight Index Average) will replace GBP LIBOR. There are key differences between GBP LIBOR and SONIA. GBP LIBOR is a 'term rate', which means that it is published for a borrowing period (such as 3 months), and it is 'forward-looking', because it is published at the beginning of the borrowing period. SONIA is currently a 'backward-looking' rate; it is based on overnight rates from actual transactions, and it is published at the end of the overnight borrowing period. Furthermore, GBP LIBOR includes a credit spread over the risk-free rate, which SONIA does not. To transition existing contracts and agreements that reference GBP LIBOR to SONIA, adjustments for term differences and credit differences might need to be applied to SONIA, to enable the two benchmark rates to be economically equivalent on transition.

At the time of reporting, industry working groups are reviewing methodologies for calculating adjustments between GBP LIBOR and SONIA.

The Group has performed an assessment of its contracts and financial instruments to determine those that reference IBOR, and associated findings have been presented to the Finance Committee. We continue to strive to promote awareness of the issue, and introduce a robust internal structure of governance and control to manage the transition. Policies and procedures will be revised where relevant to monitor any possible financial impact e.g. comparison of derivative fair values owing to differing discounting methodologies.

Additionally, we continue to closely monitor external developments in the relevant markets as rate of progress is expected to converge over the next 12 months. Of our existing contracts that directly reference IBOR, we expect transition developments to be slower in those contracts influenced by the Loan Market Association (LMA).

The amendment is mandatory and should be applied for annual periods beginning on or after 1 January 2020. Earlier application is permitted.

1 Summary of significant accounting policies (continued)

(d) Intangible assets

Intangible assets relate to software, which is written down (amortised) over the period we expect to receive a benefit from the asset, goodwill, which represents the excess of what was paid to acquire businesses over the fair value of their net assets at the acquisition date and the gas distribution Licence, which allows the operation of the four gas distribution networks.

Identifiable intangible assets are recorded at cost less accumulated amortisation and any provision for impairment. Intangible assets, other than goodwill and those assets with indefinite useful lives (the gas distribution Licence), are tested for impairment only if there is some indication that the carrying value of the assets may have been impaired.

Goodwill is recognised as an asset and is not amortised as it has been deemed that it has an indefinite life, but is tested for impairment annually or more frequently if events or changes in circumstances indicate a potential impairment. Any impairment is recognised immediately in the income statement and is not subsequently reversed.

Impairment of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash generating unit to which that asset belongs is estimated. Impairments are recognised in the income statement and are disclosed separately. Any assets which suffered impairment in a previous period (other than goodwill) are reviewed for possible reversal of the impairment at each reporting date.

Internally generated intangible assets, such as software, are recognised only if all of the following criteria are satisfied: an asset is created that can be identified; the technical feasibility of completing the intangible asset so that it will be available for use; the intention to complete the intangible asset and use it; the ability to use the intangible asset; it is probable that the asset will generate future economic benefits; the availability of adequate technical, financial and other resources to complete the development and to use the intangible asset; and that the development cost of the asset can be measured reliably. Where no internally generated intangible asset can be recognised, development expenditure is recorded as an expense in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible assets are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

Intangible assets acquired in a business combination and recognised separately from goodwill are initially recognised at their fair value at the acquisition date (which is regarded as their cost). Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

Ofgem provide the business with an exclusive right to operate, invest in the infrastructure and earn a fair return on that invested capital over a 25-year daily renewing basis governed by a comprehensive regulatory framework. On the basis that the Licence gives the owner the right to operate and invest in the gas distribution networks within the licenced geographic area, the Licence has been separately recognised and valued as part of the purchase price allocation completed in 2017. An indefinite useful economic life has been assumed for the Licence due to the daily renewing basis.

1 Summary of significant accounting policies (continued)

(d) Intangible assets (continued)
Other non-current intangible assets are amortised on a straight-line basis over their estimated useful economic lives as follows:

Amortisation Periods
Computer software - 5 years
Computer licenses - 3 years

An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognised in profit or loss when the asset is derecognised.

The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

(e) Property, plant and equipment and depreciation
The cost of these assets primarily represents the amount initially paid for them. A depreciation expense is charged to the income statement to reflect annual wear and tear and reduced value of asset over time. Depreciation is calculated by estimating the number of years we expect the asset to be used (useful economic life) and charging the cost of the asset to the income statement equally over this period.

We operate a gas distribution business and therefore have a significant physical asset base. We continue to invest in our networks to maintain reliability, create new customer connections and ensure our networks are flexible and resilient. Our business plan envisages these additional investments will be funded through a mixture of cash generated from operations and the issue of new debt.

Property, plant and equipment assets are recorded at cost, less accumulated depreciation and impairment losses. Cost includes the purchase price of the asset, any payroll and finance costs incurred which are directly attributable to the construction of property, plant and equipment assets, as well as the cost of any associated asset retirement obligations.

Property, plant and equipment assets includes assets which the Group’s interest comprises legally protected statutory or contractual rights of use. Additions represent the purchase or construction of new assets, including capital expenditure for safety and environmental assets, and extensions to, enhancements to, or replacement of existing assets.

Contributions received towards the cost of altering, diverting or relocating a tangible fixed asset are included in trade and other payables as deferred income and credited to revenue once the alteration, diversion or relocation has been completed.

Contributions received towards the cost of tangible assets from customers for connections to the gas distribution networks are initially recognised as deferred income and credited to revenue once the connection has been completed.

1 Summary of significant accounting policies (continued)

(e) Property, plant and equipment and depreciation (continued)

No depreciation is provided on freehold land or assets in the course of construction. Other items of property, plant and equipment are depreciated, on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives. In assessing the estimated useful economic lives, consideration is given to any contractual arrangements and operational requirements relating to particular assets. The assessment of estimated useful lives and residual values of assets are performed annually. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of property, plant and equipment are, in general, as shown in the table below:

Depreciation periods	Years
Freehold and leasehold buildings	Up to 50
Plant and machinery	30-50
Motor vehicles and other equipment	Up to 10

(f) Fixed asset investments

Investments in subsidiaries and associated companies are carried at cost, less any provisions for impairment.

(g) Impairment of fixed assets

Impairment reviews are carried out if there is some indication that impairment may have occurred, or where otherwise required to ensure that fixed assets are not carried above their estimated recoverable amounts. Impairments are recognised in the income statement, and, where material, are disclosed as exceptional. Impairment reversals are recognised when, in management’s opinion, the reversal is permanent.

Impairments of fixed assets are calculated as the difference between the carrying value of the net assets of income generating units, including where appropriate, investments, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value-in-use at the date the impairment review is undertaken. Net realisable value represents the amount that can be generated through the sale of assets. value-in-use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit.

(h) Financial instruments

Initial recognition

Financial assets, liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Classification and measurement

Financial instruments are classified at inception into one of the following categories which then determines the subsequent measurement methodology:

Financial assets are classified into one of the following three categories:
- financial assets at amortised cost; and
- financial assets at fair value through other comprehensive income (FVTOCI); and
- financial assets at fair value through profit or loss (FVTPL).

1 Summary of significant accounting policies (continued)

(h) Financial instruments (continued)

Classification and measurement (continued)
Financial liabilities are classified into one of the following two categories:
- financial liabilities at amortised cost; and
- financial liabilities at fair value through profit and loss (FVTPL).

Loans receivable are carried at amortised cost using the effective interest method less any allowance for estimated impairments. Impairments are calculated using the expected credit loss approach by calculating the probability of default and the estimated recoverable amount given default. A provision is established for impairments using the expected credit loss approach by calculating the probability of default and the estimated recoverable amount given default.

Borrowings, which include interest-bearing loans, are recorded at their initial fair value which normally reflects the proceeds received, net of direct issue costs less any repayments. Subsequently these are stated at amortised cost, using the effective interest method. Any difference between proceeds and the redemption value is recognised over the term of the borrowing in the income statement using the effective interest method.

Accretion on inflation linked borrowings is accounted for on an accrual basis to the income statement, and are added to the carrying value of the debt instrument to the extent that they are not settled in the period in which they arise.

Derivative financial instruments ('derivatives') are recorded at fair value. Where the fair value of a derivative is positive, it is carried as a derivative asset and where negative, as a liability.

Assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right of set off exists and the cash flows are intended to be settled on a net basis. Gains and losses arising from changes in fair value are included in the income statement in the period they arise, unless hedge accounting applies.

The fair value of financial derivatives is calculated by discounting all future cash flows by the market yield curve at the reporting date and adjusting for own and counterparty credit. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates.

For financial assets carried at amortised cost, the amount of the 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.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

Derecognition
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. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

1 Summary of significant accounting policies (continued)

(h) Financial instruments (continued)

Derecognition (continued)
On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

Impairment of financial assets
Financial assets are impaired by calculating the probability of default and the estimated recoverable amount given default, which is used to calculate the expected credit loss. The Group has taken default to be defined as a counterparty that has entered administration.

The Group recognises loss allowances for expected credit losses (ECL) on financial instruments that are not measured at FVTPL, namely:

- trade receivables; and
- loan receivables; and
- other receivables.

The Group measures the loss allowances at an amount equal to the 12 month expected credit loss. The way this is calculated is based on the applied impairment methodology, as described below:

Stage 1: For financial assets where there has not been a significant increase in credit risk since initial recognition, and were not credit impaired on recognition, the Group recognises a loss allowance based on the 12 month expected credit loss.

Stage 2: For financial assets where there has been a significant increase in credit risk since initial recognition, and were not credit impaired, the Group recognises a loss allowance for lifetime expected credit loss.

Stage 3: For financial assets which are credit impaired, the Group recognises the lifetime expected credit loss.

A significant increase in credit risk would be as a result of any change in circumstances specific to the counterparty or to the wider economic environment whereby the risk of default could be said to have been significantly increased within reasonable thresholds.

Evidence that the financial asset is credit impaired includes the following:
- significant financial difficulties of the counterparty; or
- a breach of contract such as default or past due event; or
- the restructuring of the loan or advance by the Group that the Group would not consider otherwise; or
- it is probable that the counterparty will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for an associated security because of financial difficulties.

(i) Trade receivables and accrued income
Trade receivables are amounts due from customers for goods sold or services performed in the ordinary course of business. Accrued income is amounts due from customers for goods sold or services performed in the ordinary course of business which has not yet been invoiced.

Trade receivables and accrued income are initially recognised at the transaction price and are subsequently measured at amortised cost less a loss allowance.

1 Summary of significant accounting policies (continued)

(j) Trade and other payables
Trade payables are initially recognised at amortised cost and subsequently measured at amortised cost. Due to their short maturities, the fair value of trade and other payables approximates their book values.

Deferred income mainly comprises contributions received from customers relating to capital and replacement projects. These are credited to the statement either:
• Once the project is complete; or
• Over the estimated useful economic lives of the assets to which they relate.

The treatment is dependent on the type of the project. For further detail on assessment of performance obligations see note 1(o) Revenue.

(k) Inventories
Inventories are stated at the lower of weighted average cost and net realisable value. Where applicable, cost comprises direct materials and direct labour costs as well as those overheads that have been incurred in bringing the inventories to their present location and condition.

(l) Tax
The tax charge for the period is recognised in the income statement, the statement of comprehensive income or directly in equity according to the accounting treatment of the related transaction. The tax charge comprises both current and deferred tax.

Current tax assets and liabilities are measured at the amounts expected to be recovered from or paid to the tax authorities. The tax rates and tax laws used to compute the amounts are those that have been enacted or substantively enacted by the reporting date.

The calculation of the total tax charge involves a degree of estimation and judgement, and management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes positions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred tax is provided using the balance sheet liability method and is recognised on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit or loss.

Deferred tax liabilities are generally recognised on all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences arise from the initial recognition of goodwill or from the initial recognition of other assets and liabilities in a transaction (other than a business combination) that affects neither the accounting nor the taxable profit or loss.

Deferred tax liabilities are recognised on taxable temporary differences arising on investments in subsidiaries and jointly controlled entities except where the company is able to control the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based on the tax rates and tax laws that have been enacted or substantively enacted by the reporting date.

1 Summary of significant accounting policies (continued)

(l) Tax (continued)

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred tax asset to be recovered. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same tax authorities and the company intends to settle their current tax assets and liabilities on a net basis.

(m) Provisions for liabilities

Provisions for liabilities are recognised where a legal or constructive obligation exists at the reporting date, as a result of past events where the amount of the obligation can be reliably estimated and where the outflow of economic benefit is probable.

Provision is made for decommissioning and environmental costs, based on future estimated expenditure, discounted to present values. An initial estimate of decommissioning and environmental costs attributable to property, plant and equipment is recorded as part of the original cost of the related property, plant and equipment.

Changes in the provision arising from revised estimates or discount rates or changes in the expected timing of expenditures that relate to property, plant and equipment are record as adjustments to their carrying value and depreciated prospectively over their remaining estimated useful economic lives; otherwise such changes are recognised in the income statement.

Other provisions consist of claims (whether covered by insurance or not) including employer liability claims, dilapidations and other provisions related to the operation of our gas networks. Where amounts are material, third party valuations are performed.

(n) Dividends

Dividend income is recognised when the right to receive payment is established. Dividend distributions to the company’s shareholders are recognised as a liability in the company’s financial statements in the period in which the dividends are approved by the company’s shareholders.

(o) Revenue

Revenue largely comprises sales value derived from the distribution of gas, including an assessment of the value of services provided, but not invoiced, at the period end. It excludes value added tax and intra-group sales.

The sales value for the distribution of gas is largely determined from the amount of system capacity sold for the year (capacity revenue), and the amount of gas transported for the year (commodity revenue), evaluated at contractual prices on a monthly basis. The customers for the distribution of gas are Shippers. The single performance obligation for these revenue streams was deemed to be the provision of a safe gas transportation network between the National Gas Transmission network to end consumers (customers of the shippers) and being able to transport gas around the network.

The performance obligation is satisfied over time as the gas shippers immediately control and consume the benefits that Cadent Gas provides over time by having a network available to shippers (capacity) and transporting the gas around the network (commodity). Although capacity and commodity revenue are invoiced separately, the services are not distinct (the nature of the promise is to transfer a combined service) and only one performance obligation exists.

1 Summary of significant accounting policies (continued)

(o) Revenue (continued)
Income from shippers is governed by the credit rules within the Uniform Network Code (the Industry Code by which we are bound). These set out the level of credit relative to our RAV for each counterparty's credit rating. The Group minimises customer credit risk by ensuring all customers can adequately demonstrate the ability to pay debts as they fall due. These include company credit ratings, letters of credit from a financial institution, parent company guarantees, independent assessment, payment history allowance and advanced cash deposits. Typical payment terms are 14 days.

When revenue for the year exceeds the maximum amount permitted by the regulatory agreement, adjustments will be made to future prices to reflect this over-recovery, a liability for the over-recovery is not recognised, as such an adjustment to future prices relates to the provision of future services. Similarly, an asset is not recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

Other income comprises all activities outside the regulated business principally relating to cash fees paid by customers, typically property owners / developers, for connections fees and typically developers or large infrastructure projects for altering, diverting or relocating part of our existing network. There are also non material revenue streams for call handling services (emergency telephone service for all gas distribution networks) and metering services (the provision of meter installation and repair services). For fees paid by customers the performance obligation is satisfied when either the new connection to our network or alteration / diversion of our network is completed and control passes to the customer on this completion of the physical installation ready for the first flow of gas. Significant judgement was applied for connections to determine whether the connection service was distinct from the provision of future network services. The Group judged that customers for the connection service can benefit from that connection service in conjunction with future gas supply services that are readily available. For call handling services, the performance obligation is satisfied over time with the provision of an emergency call handling service to customers. For metering services, the performance obligation is satisfied on completion of the installation or the repair and control passes when the meter is operational. Customers for metering services are typically the gas supplier and distinct from the ongoing supply of gas. Typical payment terms are 30 days for our other revenue.

(p) Exceptional items and remeasurements
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 how frequently such an event typically occurs. 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 impairment of non-current assets, integration of acquired businesses, gains or losses on disposals of businesses or investments, debt redemption costs as a consequence of transactions such as significant disposals or issues of equity and deferred tax rate changes.

Remeasurements 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 not effective. These fair values increase or decrease because of changes in financial indices and prices over which we have no control.

1 Summary of significant accounting policies (continued)

(q) Pensions

The Group operates two post-employment schemes, including both a defined benefit (DB) and a defined contribution (DC) pension scheme.

For the DC pension scheme, the Group pays contributions into separate funds on behalf of the employee and has no further obligations to employees. The risks associated with this type of plan are assumed by the member.

For the DB pension scheme, members receive benefits on retirement, the value of which is dependent on factors such as salary and length of pensionable service. The cost of providing benefits in a DB scheme is determined using the projected unit method, with actuarial valuations being carried out at each reporting date by a qualified actuary. This valuation method is an accrued benefits valuation method that makes allowance for projected earnings.

The Group's obligation in respect of DB pension plans is calculated separately for each plan by projecting the estimated amount of future benefit payments that employees have earned for their pensionable service in the current and prior periods. These future benefit payments are discounted to determine the present value of the liabilities and the fair value of plan assets and any unrecognised past service cost is then deducted. The discount rate used is the yield at the valuation date on high-quality corporate bonds with terms similar to the period over which liabilities will be paid.

The Group takes advice from independent actuaries relating to the appropriateness of key assumptions applied which include life expectancy of members, expected salary and pension increases, and inflation. It should be noted that comparatively small changes in the assumptions used may have a significant effect on the amounts recognised in the income statement and the statement of other comprehensive income and the net liability recognised in the statement of financial position.

Remeasurements of net retirement obligations are recognised in full in the period in which they occur in the statement of other comprehensive income.

(r) Leases

For the financial year beginning 1 April 2019, the Group has adopted IFRS 16 'Leases' and its policy is detailed in note 1(c).

Prior to the financial year beginning 1 April 2019, assets for use in the Group's business where the Group had substantially all the risks and rewards of ownership were classified as finance leases. Finance leases were capitalised at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments and are included in property, plant and equipment and depreciated accordingly.

The obligations related to finance leases, net of finance charges in respect of future years, were included within borrowings. The interest element of the rental obligation was charged to the income statement over the lease term so as to produce a constant periodic rate of interest on the remaining balance of the obligation for each accounting period.

Leases in which substantially all of the risks and rewards of ownership are retained by the lessor were classified as operating leases. Operating lease payments were charged to the income statement on a straight-line basis over the term of the lease.

1 Summary of significant accounting policies (continued)

(s) Cash and cash equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position.

The Group classifies cash flows as either operating, investing or financing as per the requirements of IAS 7 'Statement of cash flows'. In determining the classification the Group considers what is most appropriate to the business.

In preparing the financial statements for the 2019/20 financial year, the Group has determined that cash received in the form of capital contributions from customers, previously classified as investing activities, are more appropriately classified as cash flows from operating activities. IAS 7 defines operating activities as "the principal revenue-producing activities of the entity and other activities that are not investing or financing activities." Whilst capital contributions are received for the purpose of the creation of long-term fixed assets, the Group also generates revenue from the activity through the completion of projects to create the assets. Therefore the Group has deemed that the cash flows received from capital contributions should be classified as operating cash flows.

The cash received in the 2018/19 financial year from capital contributions was £91 million. This amount has been restated in the prior year comparative figure in the consolidated statement of cash flows. This has increased net cash generated from operations by £91 million from £1,046 million to £1,137 million and increased the net cash flows used in investing activities by £91 million from £751 million to £842 million (see the consolidated statement of cash flows).

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 period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Critical Accounting Judgements

Areas of judgement that have the most significant effect on the amounts recognised in the financial statements are as follows:

• The determination and judgement that connections and supply services are not distinct services and therefore there is only one performance obligation for revenue from the distribution of gas. We judged that customers for the connection service can benefit from that connection service in conjunction with future gas supply services that are readily available, and hence the performance obligation is distinct and revenue is recognised once the new connection is completed.

• The recognition of a surplus in respect of the defined benefit pension scheme reflects legal and actuarial advice that we have taken regarding recognition of surpluses under IFRIC 14. We have concluded that the Group has an unconditional right to a refund from the plan, in the event of a winding-up – **note 27.**

• The categorisation of certain items as exceptional items under the exceptional item framework that 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 how frequently such an event typically occurs – **note 6.**

• The allocation of goodwill to cash generating units that are expected to benefit from the business combination in which goodwill arose. We have judged that the Cadent business group is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or group of assets. Management assess the performance of Cadent business group as a single business and key decisions are currently made regarding resources at that level - **note 12.**

IFRS provides certain options available within accounting standards. We have made the choice to apply hedge accounting to financial instruments in most cases where this is permitted.

2 Critical accounting judgements and key sources of estimation uncertainty (continued)

Key Sources of Estimation Uncertainty

Key sources of estimation uncertainty that have significant risk of causing material adjustment to the carrying amounts of assets and liabilities in the next financial year are as follows:

• The impairment of intangible assets with indefinite lives requires management to calculate the value-in-use for these assets. The key assumptions for the value-in-use calculation are those regarding the underlying cash flows, discount rate, regulatory weighted average cost of capital, inflation and terminal value cash flow – **note 12.**

• Determination of useful lives and carrying values of property, plant and equipment and intangible assets. In assessing the estimated useful economic lives, consideration is given by management to any contractual arrangements and operational requirements relating to particular assets – **notes 12 & 13.**

• The estimation of liabilities for pensions and other post-retirement benefits include a number of key assumptions which include life expectancy of members, expected salary and pension increases, discount rate and inflation. The company takes advice from independent actuaries relating to the appropriateness of any key assumptions applied – **note 27.**

• In light of COVID-19 and the resulting impact on financial markets there is significant uncertainty over certain pension asset valuations, particularly of the property (£273m) and unquoted equities (£730m) portfolios as at 31 March 2020. A higher degree of caution has been attached to the property valuations received from external parties due to the unknown future impact that COVID-19 might have on the real estate market. For the property portfolio, our valuation reports from our surveyors are subject to material valuation uncertainty clauses as set out in the RICS guidance due to the impact COVID-19 has had on previous market evidence, however, we do not believe that this is likely to result in a material change in the value disclosed. For unquoted equities amounting to £54m where it was not possible to obtain valuations at 31 March 2020, a benchmark reduction based on market evidence was applied – **note 27.**

• In calculating the environmental provision a number of uncertainties affect the calculation including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies, and changes in the discount rate applied – **note 23;** and

• The estimation of the provision for claims (whether insured or not) is based on projections of liabilities that are subject to potentially large amounts of estimation, since the ultimate liability of claims is subject to the outcome of events that have not yet occurred. Examples of these events include jury decisions, court interpretations, legislative changes, changes in the medical condition of claimants, public attitudes and social/economic conditions such as inflation. In our judgement, through the use of independent actuaries we have employed techniques and assumptions that are appropriate to project the liabilities - **note 23.**

In order to illustrate the impact that changes in assumptions could have on our results and financial position, we have included sensitivity analysis in note 29.

3 Segmental analysis

The Directors believe that the whole of the Group's activities constitute one single segment. Operating segments are reported in the manner consistent with internal reporting to the Chief Operating Decision Maker, which has been identified as the Board of Directors.

The company's country of domicile is the United Kingdom and is the country in which it generates all of its revenue. The company's assets are all located within the United Kingdom.

4 Revenue

	2020	2019
	£m	£m
Revenue from distribution of gas	**1,971**	1,890
Other income	**144**	96
	2,115	1,986

Geographical analysis of revenue is not provided as the Company's operations are all undertaken in the UK for customers based in the UK.

Analysis of revenue by major customer

	2020	2019
	£m	£m
	481	480
Customer A	**209**	204
Customer B	**690**	684

One customer contributed 10% or more to the Group's revenue during the year to 31 March 2020 (2019: Two).

5 Operating profit/(loss)

	2020	2019
	£m	£m
Operating profit/(loss) is stated after charging		
Depreciation and amortisation	**390**	369
Payroll costs (see note 7)	**200**	200
Inventory consumed	**10**	13
Purchases of gas	**12**	25
Rates	**208**	204
Research and development expenditure	**7**	6
Goodwill impairment charges (see note 12)	**227**	1,372

Services provided by the company's auditor	**2020**	2019
	£'000	£'000
Audit services		
Audit of parent company and consolidated financial statements	**74**	52
Audit of subsidiary company financial statements	**657**	559
Other services		
Fees payable to the company's auditors for audit-related assurance services	**123**	118
Other non-audit services	**181**	163

Fees payable to the company's auditor for audit-related assurance services represent fees payable for services in relation to engagements which are required to be carried out by the auditor such as interim reviews. Other non-audit services in 2020 relate to services provided in connection with the raising of debt or required by the regulator.

6 Exceptional items and remeasurements

	2020 £m	2019 £m
Exceptional items included within operating costs:		
Goodwill impairment (i)	**227**	1,372
Separation activities (ii)	**19**	16
Restructuring costs (iii)	**34**	3
Guaranteed minimum pension payments (iv)	**-**	14
	280	1,405
Remeasurements included within finance costs:		
Net losses on derivative financial instruments (v)	**14**	13
Total included within profit before tax	**294**	1,418
Included within taxation:		
Exceptional charge arising		
Deferred tax charge arising as a result of the reversal of the expected reduction in the UK tax rate (vi)	**213**	-
Tax on other exceptional items and remeasurements		
Tax on separation activities	**(4)**	(3)
Tax on restructuring costs	**(6)**	(1)
Tax on guaranteed minimum pension payments	**-**	(2)
Tax on remeasurements	**(3)**	(2)
	200	(8)
Total exceptional and remeasurements after tax	**494**	1,410
Analysis of total exceptional items and remeasurements after tax		
Total exceptional items after tax	**483**	1,399
Total remeasurements after tax	**11**	11
	494	1,410

(i) A goodwill impairment was recognised in the year. This considered exceptional in nature as it is financially material and not within the Group's control. See note 12 for details.

(ii) As a result of the acquisition of Cadent Gas Limited by the company from National Grid Plc, a number of separation activities have arisen, which are exceptional by nature as this is not in the ordinary course of the business.

(iii) The Group is undergoing a reorganisation exercise. These activities are infrequent and exceptional in nature, and are financially material. On the 13 May 2019 Cadent Gas Limited announced a voluntary redundancy programme for all managers and staff. Costs of £25m associated with this have been included within restructuring costs, of which £18m relates to pension strain. A further £9m relating to consulting and project costs to support the reorganisation exercise have been incurred.

(iv) A pre-tax exceptional expense of £14m was recorded in the year ended 31 March 2019 as a past service cost in respect of the equalisation of guaranteed minimum pension ("GMP") benefits. No such amount is required for the year ended 31 March 2020.

(v) Net losses on derivative financial instruments comprise gains and losses arising on derivative financial instruments reported in the income statement. These exclude gains and losses for which hedge accounting has been effective, which have been recognised directly in other comprehensive income or which are offset by adjustments to the carrying value of debt.

(vi) The resolution moved by the Chancellor of the Exchequer that the Corporation tax rate for financial year 2020 and 2021 shall be 19% was given statutory effect under the provisions of the Provisional Collection of Taxes Act 1968 on 11 March 2020 and therefore on the basis that this rate will apply for the foreseeable future deferred tax has been restated from 17% of temporary differences to 19% of temporary differences. As this is an infrequent adjustment that was out of the Group's control and financially material it has been recognised as an exceptional cost.

7 Employment costs

The average number of persons (including Executive Directors) employed by the Group was 3,938 (2019: 4,062).

	2020	2019
Field force	**1,690**	1,726
Office and other administrative staff	**2,248**	2,336
	3,938	4,062

	2020	2019
	£m	£m
Wages and salaries	**182**	182
Social security costs	**22**	22
Other pension costs	**54**	52
	258	256
Less: payroll costs capitalised	**(58)**	(56)
	200	200

Key management compensation

Key management comprises the Board of Directors of the company and its principle subsidiary, Cadent Gas Limited, including Executive and Non-executive Directors who have managerial responsibilities of the business.

	2020	2019
	£'000	£'000
Salaries and other short-term employee benefits	**1,985**	1,699
Post-employment benefits	**102**	130
	2,087	1,829

8 Directors' emoluments

The Directors' emoluments were as follows:

	2020	2019
	£'000	£'000
Aggregate emoluments (including salary, fees, bonuses and benefits in kind)	**1,985**	1,699
Pension schemes	**102**	130
	2,087	1,829

There were no amounts paid to third parties for Directors' services.

Post-employment benefits were being accrued for Nil (2019: one) Directors under a defined benefit scheme.

Highest paid Director

The highest paid Director's emoluments for the Group were as follows:

	2020	2019
	£'000	£'000
Total amount of emoluments and amounts receivable (excluding shares) under long-term incentive schemes	**786**	804
Defined benefit pension scheme		
- accrued pension at end of period	**60**	75

9 Finance income and costs

	2020 £m	2019 £m
Finance income		
Pension interest income	**17**	14
Interest income from financial instruments	**1**	2
Finance income	**18**	16
Finance costs		
Interest expense on financial liabilities held at amortised cost:		
Bank loans and overdrafts	**34**	47
Other borrowings	**181**	149
Interest payable on intercompany financing	**60**	59
Derivatives	**5**	9
Unwinding of discounts on provisions and lease liabilities	**1**	-
Finance costs	**281**	264
Remeasurements		
Net gains/(losses) on derivative financial instruments included in remeasurements (i):		
Ineffectiveness on derivatives designated as:		
Cash flow hedges	**(1)**	(5)
Derivatives not designated as hedges or ineligible for hedge accounting	**15**	18
Remeasurements included within finance costs	**14**	13
Finance costs	**295**	277
Net finance costs	**277**	261

i) Includes a net foreign exchange loss on financing activities of £36m (2019: £5m gain). These amounts are offset by foreign exchange gains and losses on derivative financial instruments measured at fair value.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2020

10 Taxation

Tax charged/(credited) to the income statement

	2020	2019
	£m	£m
Tax before exceptional items and remeasurements	**128**	98
Exceptional tax relating to UK tax rate change (see note 6)	**213**	-
Tax on other exceptional items and remeasurements	**(13)**	(8)
Total tax expense	**328**	90

	2020	2019
	%	%
Before exceptional items and remeasurements	**19.2**	18.4
After exceptional items and remeasurements	**88.2**	(10.2)

The tax charge for the year can be analysed as follows:

	2020	2019
	£m	£m
Current tax		
UK corporation tax at 19% (2019: 19%)	**119**	110
UK corporation tax adjustment in respect of prior years	**1**	(3)
Total current tax	**120**	107
Deferred tax		
UK deferred tax current year	**(5)**	(15)
UK deferred tax arising as a result of the reversal of the expected reduction in the UK tax rate	**213**	-
UK deferred tax adjustment in respect of prior years	**-**	(2)
Total deferred tax	**208**	(17)
Total tax charge	**328**	90

Tax charged/(credited) to other comprehensive income and equity

	2020	2019
	£m	£m
Deferred tax		
Accelerated tax depreciation	**-**	1
Cash flow hedges	**(3)**	-
Remeasurements of net retirement benefit obligations (i)	**46**	23
Total tax charged to other comprehensive income and equity	**43**	24

(i) £13m relates to tax arising as a result of the reversal of the expected reduction in the UK tax rate.

The tax charge for the period after exceptional items and remeasurements is higher (2019: lower) than the standard rate of corporation tax in the UK of 19% (2019: 19%).

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2020

10 Taxation (continued)

	Before exceptional items and Remeasure-ments 2020 £m	**After exceptional items and Remeasure-ments 2020 £m**	Before exceptional items and Remeasure-ments 2019 £m	After exceptional items and Remeasure-ments 2019 £m
Profit/(loss) before tax				
Before exceptional items and remeasurements	**666**	**666**	534	534
Exceptional items and remeasurements	**-**	**(294)**	-	(1,418)
Profit/(loss) before tax	**666**	**372**	534	(884)
Profit before tax multiplied by UK corporation tax rate of 19% (2019: 19%)	**127**	**71**	101	(168)
Effect of:				
Expenses not deductible for tax purposes	**2**	**45**	4	265
Non-taxable income	**(2)**	**(2)**	(1)	(1)
Corporation tax/deferred tax rate differential	**-**	**-**	(1)	(1)
Deferred tax impact of change in UK tax rate	**-**	**213**	-	-
Prior year adjustments	**1**	**1**	(5)	(5)
Total tax	**128**	**328**	98	90

Factors that may affect future tax charges

The resolution moved by the Chancellor of the Exchequer that the Corporation tax rate for financial year 2020 and 2021 shall be 19% was given statutory effect under the provisions of the Provisional Collection of Taxes Act 1968 on 11 March 2020 and therefore deferred tax has been restated to 19% of temporary differences. The tax impact of the new accounting standard IFRS 16 Leases will not be material for the foreseeable future.

10 Taxation (continued)

Taxation included within the statement of financial position

The following are the major deferred tax assets and liabilities recognised, and the movements thereon, during the current and prior reporting periods:

	Accelerated Tax Depreciation £m	**Gas Distribution License £m**	**Pensions £m**	**Financial Instruments £m**	**Other net Temporary Differences £m**	**Total £m**
At 1 April 2019	**1,462**	**364**	**117**	**(5)**	**(10)**	**1,928**
Charged/(credited) to income statement	**160**	**43**	**9**	**(3)**	**(1)**	**208**
Charged/(credited) to other comprehensive income and equity	**-**	**-**	**46**	**(3)**	**-**	**43**
At 31 March 2020	**1,622**	**407**	**172**	**(11)**	**(11)**	**2,179**
Deferred tax assets at 31 March 2020	**-**	**-**	**-**	**(11)**	**(11)**	**(22)**
Deferred tax liabilities at 31 March 2020	**1,622**	**407**	**172**	**-**	**-**	**2,201**
At 31 March 2020	**1,622**	**407**	**172**	**(11)**	**(11)**	**2,179**

	Accelerated Tax Depreciation £m	Gas Distribution License £m	Pensions £m	Financial Instruments £m	Other net Temporary Differences £m	Total £m
At 1 April 2018	1,481	364	82	(4)	(2)	1,921
Charged/(credited) to income statement	(20)	-	12	(1)	(8)	(17)
Credited to other comprehensive income and equity	1	-	23	-	-	24
At 31 March 2019	1,462	364	117	(5)	(10)	1,928
Deferred tax assets at 31 March 2019	-	-	-	(5)	(10)	(15)
Deferred tax liabilities at 31 March 2019	1,462	364	117	-	-	1,943
At 31 March 2019	1,462	364	117	(5)	(10)	1,928

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net. The deferred tax balances (after offset) for statement of financial position purposes consist solely of deferred tax liabilities of £2,179m (2019: £1,928m).

11 Dividends

	2020	2019
	£000	£000
Interim dividend of 3.33 pence per ordinary share amounting to £170,000,000 was declared and paid on the 28 September 2018	**-**	170,000
Second interim dividend of 3.33 pence per ordinary share amounting to £170,000,000 was declared on the 21 March 2019 and paid on the 27 March 2019	**-**	170,000
Interim dividend of 2.69 pence per ordinary share amounting to £137,350,000 was declared and paid on the 27 September 2019	**137,350**	-
Second interim dividend of 2.69 pence per ordinary share amounting to £137,350,000 was declared on the 19 March 2020 and paid on the 23 March 2020	**137,350**	-
	274,700	340,000

No further dividends are proposed for the current financial period.

12 Intangible assets

	Goodwill	**Licence**	**Software**	**Total**
	£m	**£m**	**£m**	**£m**
Cost:				
At 1 April 2019	3,312	2,143	120	5,575
Additions	-	-	46	46
At 31 March 2020	**3,312**	**2,143**	**166**	**5,621**
Accumulated amortisation and impairment				
At 1 April 2019	(1,372)	-	(57)	(1,429)
Amortisation charge for the year	- -	-	(19)	(19)
Impairment	(227)	-	-	(227)
At 31 March 2020	**(1,599)**	**-**	**(76)**	**(1,675)**
Net book value:				
At 31 March 2020	**1,713**	**2,143**	**90**	**3,946**
At 31 March 2019	1,940	2,143	63	4,146

12 Intangible assets (continued)

	Goodwill £m	Licence £m	Software £m	Total £m
Cost:				
At 1 April 2018	3,312	2,143	90	5,545
Additions	-	-	30	30
At 31 March 2019	3,312	2,143	120	5,575
Accumulated amortisation:				
At 1 April 2018	-	-	(31)	(31)
Amortisation charge for the year	-	-	(26)	(26)
Impairment	(1,372)	-	-	(1,372)
At 31 March 2019	(1,372)	-	(57)	(1,429)
Net book value:				
At 31 March 2019	1,940	2,143	63	4,146
At 31 March 2018	3,312	2,143	59	5,514

On 31 March 2017, Quadgas MidCo Limited acquired 100% of the share capital of Cadent Gas Limited including its subsidiary, Cadent Finance Plc, and 100% of the share capital of Cadent Services Limited for £7,744 million, funded through intercompany loans from its parent company and external borrowings. At the time, the Group applied IFRS 3 ‘Business Combinations’ and the acquisition was accounted for using the acquisition method with the difference between the fair value of the consideration and the fair value of the net assets acquired recognised as goodwill. As part of this purchase price allocation exercise, goodwill of £3,312m was recognised together with an intangible for the gas distribution Licence of £2,143m.

Ofgem provide the business with an exclusive right to operate, invest in the infrastructure and earn a fair return on that invested capital over a 25-year daily renewing basis governed by a comprehensive regulatory framework. On the basis that the Licence gives the owner the right to operate and invest in the gas distribution networks within the licenced geographic area, the Licence has been separately recognised and valued as part of the purchase price allocation. An indefinite useful economic life has been assumed for the Licence due to the daily renewing basis.

Goodwill encompasses the management related portion of incentive income, an element of financial outperformance, the benefit of a clean capital structure on acquisition and the established workforce.

Goodwill is recognised as an asset and is not amortised but is tested for impairment annually or more frequently if events or circumstances indicate a potential impairment. Any impairment is recognised immediately in the income statement and is not subsequently reversed.

Goodwill is allocated to cash generating units that are expected to benefit from the business combination in which goodwill arose. The cash generating unit has been determined as the level of Cadent Gas Limited. Cadent was assessed to be a single reporting segment, since management assess the performance of Cadent as a single business and key decisions are made regarding resources at the Cadent level. This was considered to be the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or group of assets.

12 Intangible assets (continued)

Impairment Testing of goodwill and intangibles with an indefinite life

During the year, management completed the annual impairment test required for the goodwill and indefinite life intangibles that it holds on its balance sheet. The impairment test required the comparison of the carrying value of the net assets of the income generating unit (Cadent Gas Limited) and its recoverable amount. The impairment review was completed following receipt of the Ofgem Draft Determinations on 9 July 2020 as the RIIO-2 settlement has the potential to impact on the future cash flows and recoverable amount. The Draft Determinations included a challenging draft set of proposals, indicating the possibility of a further impairment arising over and above the impairment booked in the prior year following the publication by Ofgem of the RIIO-2 Sector Specific Methodology. Additionally, management considered the potential short and long-term impacts of COVID-19 and have incorporated any risks identified into the impairment test.

This calculation indicated that the recoverable amount was lower than the carrying amount and an impairment charge of £227m (2019: £1,372m) was recognised within exceptional items in the income statement. Under the requirements of IAS 36, this impairment was allocated to the goodwill balance of the cash generating unit (the business of gas distribution at the total Cadent business group level - the level at which the performance of the Cadent business group is managed and at which key decisions are currently made regarding resources) and an impairment loss of £227m (2019: £1,372m) was recognised against the goodwill balance.

The recoverable amount of the cash generating unit was determined from value-in-use calculations. The key assumptions for the value-in-use calculation are those regarding the underlying cash flows, discount rate, inflation and terminal value cash flow.

Underlying cash flows

In the short-term, the differences between actual cash flows and prior projections/budgets are small due to the stable and predictable nature of the business. With 93% of our revenue formula driven, there is a high level of predictability. This predictability of the cash flows was seen in the full year performance to 31 March 2020 where our results were broadly in line with our budget.

The total expenditure (totex) forecasts included in our impairment model are a base case and assume the investment in the network will continue to 2045 and beyond. However, the base case does not include cash flows associated with the potential to re-purpose the network for hydrogen or other fuels. In the base case we continue to assume regulatory asset depreciation of 45 years and investment is fully capitalised into the RAV. This is consistent with the Ofgem Draft Determinations proposed methodology.

We have determined the regulated weighted average cost of capital (WACC) using the ranges set out in Ofgem's Draft Determination. The regulatory cost of equity per the Draft Determination (range of low 3.6% to high 4.8%) is forecast to increase in future price controls consistent with assumptions adopted in the prior year.

Management also considered the impact of COVID-19 on the long-term performance of the business. Despite operational and cost impacts in the short-term, the impact on long-term value was deemed to be limited concerning the operations of the business due to the stable regulatory framework of UK utilities and the engagement with Ofgem regarding the consequences of COVID-19. We are currently discussing with Ofgem how any potential under-performance against RIIO-1 regulatory targets will be managed but have assumed in our forecasts that Ofgem will act reasonably when considering any potential adverse implications.

12 Intangible assets (continued)

Discount rate

Cash flow projections have been discounted to reflect the time value of money, using a pre-tax discount rate of 5.0% (2019: 5.7%). Management estimates the discount rate using post-tax rates that reflect current market assessments of the time value of money and then converts to a pre-tax rate using an iterative calculative approach in the value-in-use methodology. The reduction in discount rate from prior year is driven by a lower risk free rate (we have changed our approach from last year from using a spot forward rate at 31 March to take a view of the risk free rate through the financial year to normalise the impact of COVID-19 at the end of the financial year) and amendments to the risk premium to ensure the appropriate incorporation of risk within the cash flows and the discount rate.

Inflation

The short-term RPI assumption to March 2021 of 2.5% (2019: 3.25%) is based on the average RPI forecast at the time of completing the short-term Business Plan in January 2020. The current view is that the inflation in the year to March 2021 will be lower, however, we do not consider this to be material to long-term value.

The long-term CPI assumption of 2.0% (2019: 2.15%) is consistent with the Bank of England target rate and external long run forecasts which show a range of potential outcomes between 1.4% - 2.3% by 2024. Given the range of potential outcomes, this year, we have adopted the Bank of England target of 2.0% as our long run CPI assumption from 2022 to 2045.

Terminal value cash flow

A terminal value cash flow is applied in 2045; the end of the forecast period. The terminal value is calculated based on a RAV forecast multiple at 2045. Management has derived a RAV multiple of 1.2x (2019: 1.2x) by reviewing external sources of information on similar transactions. There has been no change in the market to warrant a revision to this assumption.

IAS 36 states that projections based on budgets and forecasts should cover a maximum of five years whereas management have used projections out to 2045. However, management of Quadgas Midco Limited believe, whilst there is uncertainty when moving from one price control period in to the next, there is otherwise a degree of predictability to the cash flows of the assets and therefore management consider that it is appropriate to project out to 2045 before a terminal value is applied.

Further sensitivity and key assumptions are included in note 29.

13 Property, plant and equipment

	Land and buildings £m	Plant and Machinery £m	Assets in the course of construction £m	Motor vehicles and other equipment £m	Right-of -use assets* £m	Total £m
Cost						
At 1 April 2019	89	11,348	80	124	-	11,641
Initial application of IFRS 16	-	-	-	-	26	26
Additions	6	693	93	18	5	815
Reclassifications	16	53	(73)	(1)	5	-
Disposals	(1)	(1)	-	(3)	-	(5)
At 31 March 2020	**110**	**12,093**	**100**	**138**	**36**	**12,477**
Accumulated depreciation and impairment						
At 1 April 2019	(14)	(602)	-	(48)	-	(664)
Charge for the period	(8)	(332)	-	(24)	(7)	(371)
Disposals	-	-	-	2	-	2
At 31 March 2020	**(22)**	**(934)**	**-**	**(70)**	**(7)**	**(1,033)**
Net book value:						
At 31 March 2020	**88**	**11,159**	**100**	**68**	**29**	**11,444**
At 31 March 2019	75	10,746	80	76	-	10,977

Depreciation has been calculated on a straight-line basis over the estimated useful life of the asset. In assessing the estimated useful economic lives, management give consideration to any contractual arrangements and operational requirements relating to particular assets. See note 1(e) for the estimated useful lives of each asset category, and note 29 for sensitivity analysis over the residual lives of assets.

Included within plant and machinery cost is £1,785m (2019: £1,785m) and plant and machinery depreciation is £145m (2019: £96m) relating to fair value adjustments arising from the acquisition of Cadent Gas Limited.

The cost of property, plant and equipment at 31 March 2020 includes £1,462,000 (2019: £1,462,000) relating to interest capitalised, with £Nil (2019: £Nil) capitalised during the year.

Additions to the right-of-use assets during the 2019/20 financial year were £5m.

The net book value of right-of-use assets comprises:

	31 March 2020 £m	1 April 2019* £m
Land and buildings	**17**	20
Plant and machinery	**1**	1
Motor vehicles and other equipment	**11**	10
	29	31

*In the previous year, the Group only recognised leased assets in relation to leases that were classified as 'finance leases' under IAS 17 'Leases'. For adjustments recognised on adoption of IFRS 16 on 1 April 2019, refer to note 1(c). Both right-of-use assets and assets initially recognised in previous periods under IAS 17 are included in property, plant and equipment in the consolidated statement of financial position.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2020

13 Property, plant and equipment (continued)

The net book value of land and buildings comprises:

	2020	2019
	£m	£m
Freehold	**71**	53
Long leasehold (over 50 years)	**-**	-
Short leasehold (under 50 years)	**17**	22
	88	75

	Land and buildings	Plant and Machinery	Assets in the course of construction	Motor vehicles and other equipment	Total
	£m	£m	£m	£m	£m
Cost					
At 1 April 2018	83	10,736	20	98	10,937
Additions	6	606	74	20	706
Reclassifications	-	7	(14)	7	-
Disposals	-	(1)	-	(1)	(2)
At 31 March 2019	89	11,348	80	124	11,641
Accumulated depreciation and impairment					
At 1 April 2018	(7)	(293)	-	(23)	(323)
Charge for the period	(7)	(310)	-	(26)	(343)
Disposals	-	1	-	1	2
At 31 March 2019	(14)	(602)	-	(48)	(664)
Net book value:					
At 31 March 2019	75	10,746	80	76	10,977
At 31 March 2018	76	10,443	20	75	10,614

14 Investments in associates

The Group's only associate is in respect of its 45.57% equity stake in Xoserve Limited, which was previously fully impaired.

	Total £m
Cost	
At 1 April 2019 & 31 March 2020	-
Provision	
At 1 April 2019 & 31 March 2020	-
Net book value:	
At 1 April 2019 & 31 March 2020	**-**

At the point of acquiring Cadent Gas Limited on 31 March 2017, its investment in Xoserve Limited of £456 had been fully impaired.

Details of the associate undertaking are set out below:

Company	Class of share held	Place of business and country of incorporation	Percentage held	Principal activities
Xoserve Limited	Convertible redeemable, ordinary share of £0.01 designated as an A Share in the capital of the company	Registered address Lansdowne Gate, 65 New Road, Solihull, B91 3DL. Incorporated in England and Wales.	45.57%	Gas transportation transaction services

Outstanding balances with associates are shown in note 31.

15 Inventories

	2020 £m	2019 £m
Raw materials and consumables	**10**	10
	10	10

Inventories are stated after provisions for impairment of £909,000 (2019: £307,000).

16 Trade and other receivables

	2020	2019
	£m	£m
Amounts falling due within one year:		
Trade debtors	**10**	16
Other debtors	**20**	12
Prepayments	**37**	25
Accrued income	**173**	166
	240	219
Amounts falling due after more than one year:		
Prepayments	**6**	29
Other debtors	**15**	15
	21	44

In determining the recoverability of trade and other receivables the Group considers any change in credit worthiness of the counterparty from the date credit was initially granted up to the reporting date.

The movement in loss allowance for the year was as follows:

	2020	2019
	£m	£m
At 1 April	**3**	4
Amounts utilised/written off in the year	**-**	-
Amounts credited to the income statement	**-**	(1)
At 31 March	**3**	3

When judging if a financial asset should be valued using the lifetime expected loss calculation the Group needs to assess if there has been a significant increase in credit risk.

The Group takes a simplified approach and considers all receivables to be in stage 2 immediately. When assessing if a financial asset has reached level 3 (credit impaired), the following information is considered:

- existing or anticipated adverse changes in economic conditions that are expected to lead to a significant decrease in the counterparty’s ability to meet its debt obligations;
- actual or expected significant reduction of the profitability of the counterparty; and
- significant movement in credit risk derived from observable market data relating to the same or similar counterparty.

The Group has assessed whether there is any impact of COVID-19 on the recoverability of trade and other receivables. The impact was deemed to be limited given the nature of the business in that our principal commercial exposure relates to shipper income which is governed by Section V of the Gas Transportation Uniform Network Code. There are a number of actions the Group takes to mitigate credit risks and any changes to the Uniform Network Code will need to be agreed across the gas industry with involvement from Ofgem. These include holding security in the form of cash, obtaining letters of credit and ensuring major diversionary work is invoiced in advance of the work commencing.

The impairment under the expected credit loss has been calculated by grouping customers into two distinct segments with significantly different customer bases and customer credit profiles. These segments are distinguished as follows:

- Other income: diversions receivables, damages receivables, emergencies receivables, and other receivables.
- Shipper income: capacity accrued income, commodity accrued income.

16 Trade and other receivables (continued)

Other Income

Other income included within trade debtors relates to any income stream which involves rechargeable construction work done on the network where the costs can be charged to another party. Examples include diversions income would be diversions of gas pipes, charges for damages to gas pipes and rechargeable emergency repairs.

The loss allowance of the receivable balance is calculated using the expected loss model, and is calculated using a matrix based on the number of days past due plus any specific adjustments. Specific adjustments have been made based on forward looking information specific to any counterparty or counterparty segment which would lead the Group to adjust the normal matrix based calculation.

2020	**Not due £m**	**Current £m**	**1-6 months £m**	**6-12 months £m**	**Over 1 year £m**	**Total £m**
Total balance	**4**	**-**	**1**	**1**	**7**	**13**
Expected credit loss	**-**	**-**	**(1)**	**-**	**(2)**	**(3)**
Balance after loss allowance	**4**	**-**	**-**	**1**	**5**	**10**

2019	Not due £m	Current £m	1-6 months £m	6-12 months £m	Over 1 year £m	Total £m
Total balance	6	3	2	1	7	19
Expected credit loss	-	-	(1)	-	(2)	(3)
Balance after loss allowance	6	3	1	1	5	16

Shipper Income

Shipper income relates to all income received from gas shippers and is included within accrued income. These amounts relate to two different elements, capacity and commodity income. Typically shippers will settle within 14 days.

The Group minimises customer credit risk by ensuring all customers can adequately demonstrate the ability to pay debts as they fall due. These include company credit rating, letter of credit from a financial institution, parent company guarantee, independent assessment, payment history allowance and advanced cash deposits.

The shippers are required to pay on strict schedules and failure to pay on the predetermined date will result in sanctions being placed on the customer account which are designed to reduce the Group's risk, such as refusal to give more credit.

Due to the credit risk control practices outlined above the Group expects to be able to reduce the credit exposure to near zero before any shipper customer balances becomes level 3.

2020	**Not due £m**	**Current £m**	**1-6 months £m**	**6-12 months £m**	**Over 1 year £m**	**Total £m**
Total balance	**173**	-	-	-	-	**173**
Expected credit loss	-	-	-	-	-	**-**
Balance after loss allowance	**173**	**-**	**-**	**-**	**-**	**173**

2019	Not due £m	Current £m	1-6 months £m	6-12 months £m	Over 1 year £m	Total £m
Total balance	166	-	-	-	-	166
Expected credit loss	-	-	-	-	-	-
Balance after loss allowance	166	-	-	-	-	166

17 Derivative financial instruments

The fair values of derivative financial instruments are as follows:

	2020		
	Assets £m	**Liabilities £m**	**Total £m**
Amounts falling due within one year	**-**	**-**	**-**
Amounts falling due after more than one year	**44**	**(73)**	**(29)**
	44	**(73)**	**(29)**

	2019		
	Assets £m	Liabilities £m	Total £m
Amounts falling due within one year	-	-	-
Amounts falling due after more than one year	8	(38)	(30)
	8	(38)	(30)

For each class of derivative the notional contract amounts* are as follows:

	2020 £m	2019 £m
Cross-currency interest rate swaps	**1,337**	895
Inflation linked swaps	**400**	400
Foreign exchange forward currency	**4**	-
	1,741	1,295

*The notional contract amounts of derivatives indicate the gross nominal value of transactions outstanding at the reporting date.

18 Current asset investments

	2020 £m	2019 £m
Investments in short-term money funds	**332**	339
	332	339

19 Trade and other payables

	2020	2019
	£m	£m
Trade creditors	**280**	276
Amounts owed to immediate parent company	**1**	-
Other tax and social security	**59**	45
Other creditors	**56**	28
Accruals and deferred income	**198**	211
	594	560

Due to the short-term nature of trade creditors, the fair value approximates its book value.

20 Accruals and deferred income

	2020	2019
	£m	£m
Accruals and deferred income (due after more than one year)	**12**	27
	12	27

Accruals and deferred income mainly comprises fees received from customers for capital projects.

21 Borrowings

	2020	2019
	£m	£m
Amounts falling due within one year		
Bank loans	**75**	2
Bank overdrafts	**8**	9
Bonds	**56**	54
Finance leases under IAS 17*	**-**	1
	139	66
Amounts falling due after more than one year		
Bank loans	**1,449**	1,538
Bonds	**7,415**	7,031
Amounts owed to parent company	**902**	902
Finance leases under IAS 17*	**-**	5
	9,766	9,476

*Due to the adoption of IFRS 16 'Leases', lease liabilities for the year ended 31 March 2020 are now shown separately to borrowings within the financial statements. Comparative information has not been restated. See note 1(c) and note 22.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2020

21 Borrowings (continued)

	2020*	2019*
	£m	£m
Total borrowings are repayable as follows:		
Less than 1 year	**139**	66
In 1-2 years	**242**	-
In 2-3 years	**-**	1,250
In 3-4 years	**91**	-
In 4-5 years	**1,651**	91
More than 5 years	**7,782**	8,135
	9,905	9,542

*Due to the adoption of IFRS 16, in the current financial year we have presented lease liabilities as a separate line item in the consolidated statement of financial position, therefore lease liabilities are not included above for the current year. As comparatives have not been restated under IFRS 16, the prior year figures still include finance lease liabilities under IAS 17.

On 12 July 2019 Cadent Gas Ltd, a subsidiary of Quadgas MidCo Limited, refinanced its outstanding debt facilities extending the maturity to 2024 (previously 2021). This included repaying the existing syndicated term loan of £393m and drawing a new syndicated term loan of £300m. The undrawn Revolving Credit Facility of £500m was replaced to extend the maturity to 2024.

On 12 July 2019, Quadgas Midco Ltd refinanced its outstanding debt facilities extending the maturity to 2024 (previously 2022). This included repaying the existing syndicated term loan of £218m and drawing a new syndicated term loan of £220m. The Revolving Credit Facility of £380m was replaced with a new facility of £200m with maturity date of 2024, as was the liquidity facility. £70m of the Revolving Credit Facility was drawn as at 31 March 2020.

On 10 October 2019, Cadent Finance Plc, a subsidiary of Quadgas MidCo Limited, issued a 16 year fixed rate bond with a notional value of £300m and a coupon of 2.25% under its £6bn Euro Medium Term Note Programme, this bond is guaranteed by and proceeds were on lent to Cadent Gas Limited.

On 11 October 2019, Cadent Finance Plc repurchased and cancelled £400m notional value of notes, under a Tender Offer launched on 1 October 2019. The notes repaid were part of the £650m 2021 maturity notes issued in 2016; this leaves £250m of this issue outstanding.

On 11 March 2020, Cadent Finance Plc issued a 12 year fixed rate transition bond with a notional value of €500m and a coupon of 0.75% under its £6bn Euro Medium Term Note Programme, this bond is guaranteed by and proceeds were on lent to Cadent Gas Limited. This was swapped to c.£436m and a rate of 1.81% immediately on issue.

The fair value of borrowings at 31 March 2020 was £9,824m. Where market values were available, the fair value of borrowings (Level 1) was £4,641m. Where market values were not available, the fair value of borrowings (Level 2) was £5,183m, calculated by discounting cash flows at prevailing interest rates. The notional amount of borrowings outstanding as at 31 March 2020 was £9,213m (2019: £8,901m), £9,530m (2019: £9,171m) including accretion.

21 Borrowings (continued)

Summary of Borrowings

Currency	Type	Notional* £m	Rate	Maturity Date	Book value £m	Fair Value £m
Fixed Rate						
GBP	Listed	250	Fixed	22/09/2021	243	249
EUR**	Listed	643	Fixed	22/09/2024	655	656
GBP	Listed	850	Fixed	22/09/2028	850	852
GBP	Listed	700	Fixed	22/09/2038	694	706
GBP	Listed	800	Fixed	22/09/2046	799	802
GBP	Listed	300	Fixed	21/03/2040	295	318
JPY***	Listed	68	Fixed	19/07/2033	76	69
GBP	Listed	300	Fixed	10/10/2035	298	290
EUR*****	Listed	439	Fixed	11/03/2032	437	406
GBP	Listed	100	Fixed	19/03/2031	101	105
USD****	Listed	151	Fixed	19/03/2031	161	169
GBP	Listed	200	Fixed	19/03/2034	199	211
GBP	Listed	225	Fixed	19/03/2039	224	238
GBP	Listed	125	Fixed	31/03/2037	126	130
GBP	Unlisted	902	Fixed	31/03/2037	902	902
GBP	Listed	149	Fixed	31/10/2027	151	149
GBP	Listed	103	Fixed	31/10/2029	103	103
GBP	Listed	40	Fixed	31/10/2032	40	40
USD******	Listed	38	Fixed	31/10/2024	40	41
GBP	Listed	70	Fixed	30/08/2030	71	71
GBP	Listed	225	Fixed	30/08/2033	227	231
GBP	Listed	350	Fixed	17/09/2029	352	362
		7,028			**7,044**	**7,100**
Index-linked						
GBP	Unlisted	82	RPI-linked	02/10/2023	92	88
GBP	Unlisted	82	RPI-linked	18/06/2024	88	84
GBP	Unlisted	82	RPI-linked	25/06/2024	88	85
GBP	Unlisted	82	RPI-linked	29/04/2024	89	86
GBP	Unlisted	82	RPI-linked	30/04/2024	88	86
GBP	Unlisted	82	RPI-linked	07/05/2024	88	86
GBP	Listed	146	RPI-linked	02/05/2039	234	225
GBP	Listed	150	RPI-linked	10/08/2048	266	257
GBP	Listed	150	RPI-linked	14/08/2048	261	253
GBP	Listed	286	RPI-linked	31/03/2042	284	263
GBP	Listed	43	RPI-linked	31/03/2037	42	42
GBP	Listed	80	RPI-linked	31/03/2042	82	70
GBP	Listed	80	RPI-linked	31/03/2037	82	76
		1,427			**1,784**	**1,701**
Floating Rate						
GBP	Unlisted	300	LIBOR +	11/07/2024	300	289
GBP	Unlisted	400	LIBOR +	27/03/2027	400	376
GBP	Listed	77	LIBOR +	31/03/2037	78	68
GBP	Unlisted	220	LIBOR +	11/07/2024	221	212
GBP	Listed	70	LIBOR +	18/06/2020	70	70
		1,067			**1,069**	**1,015**
Overdraft		**8**			**8**	**8**
TOTAL		**9,530**			**9,905**	**9,824**

* Index-linked debt notional is the accreted value
** EUR amount is €750m
*** JPY amount is ¥10bn
**** USD amount is $200m
***** EUR amount is €500m
****** USD amount is $50m

22 Lease liabilities

a) Amounts recognised in the balance sheet

	2020	1 April 2019*
	£m	£m
Current	**9**	7
Non-current	**18**	22
	27	29

*In the previous year, the Group only recognised lease liabilities in relation to leases that were classified as 'finance leases' under IAS 17 Leases. These were presented as part of the Group's borrowings. For adjustments recognised on adoption of IFRS 16 on 1 April 2019, please refer to note 1(c).

	2020
Lease liabilities are repayable as follows:	**£m**
Year 1	**9**
Year 2	**5**
Year 3	**3**
Year 4	**2**
Year 5	**1**
Onwards	**7**
	27

The Group does not face a significant liquidity risk with regard to its lease liabilities. See note 28 (financial risk management) for further analysis.

The below comparatives are the finance lease liabilities and operating lease commitments under IAS 17.

	Minimum lease payments 2019 £m
Amounts payable under finance leases:	
Within one year	1
In the second to fifth years inclusive	4
After five years	2
Less: future finance charges	(1)
Present value of lease obligations	6

Obligations under finance leases

	Present Value of Minimum lease payments 2019 £m
Amounts payable under finance leases:	
Within one year	1
In the second to fifth years inclusive	3
After five years	2
Present value of lease obligations	6
Analysed as:	
Amounts due for settlement within 12 months (shown under current liabilities)	1
Amounts due for settlement after 12 months	5
	6

22 Lease liabilities (continued)

The Group had the following future minimum lease payments under non-cancellable operating leases for each of the following periods:

	2019
	£m
Less than one year	7
In two-five years	11
More than five years	9
	27

See reconciliation of operating lease commitments disclosed at 31 March 2019 to lease liabilities recognised at 1 April 2019 in note 1 (c).

All lease liabilities are denominated in sterling.

b) Amounts recognised in the statement of profit or loss

	2020
	£m
Depreciation of right-of-use assets (see note 13)	**7**
Expense relating to short-term leases (included within operating expenses)	**2**
Expense relating to leases of low-value assets that are not short-term leases (included within operating expenses)	**–**
Expense relating to variable lease payments not included in lease liabilities (included within operating expenses)	**10**

The total cash outflow for leases for the year ended 31 March 2020 was £7m.

23 Provisions for liabilities

	Decommissioning £m	Environmental £m	Other £m	Total £m
At 1 April 2019	4	40	51	95
Charged to the income statement	-	-	22	22
Utilised	(2)	(1)	(10)	(13)
Released to the income statement	-	-	(1)	(1)
Unwinding of discount	-	-	-	-
At 31 March 2020	**2**	**39**	**62**	**103**

	Decommissioning £m	Environmental £m	Other £m	Total £m
Current	2	2	12	16
Non-current	-	37	50	87
	2	**39**	**62**	**103**

Decommissioning provision

The decommissioning provision represents expenditure relating to the demolition of gas storage facilities expected to be incurred until 2021.

Environmental provision

The environmental provision represents the estimated restoration and remediation costs relating to old gas manufacturing sites owned by the Group (discounted using a real rate of 1% (2019: 1.0%)). Cash flows are expected to be incurred between 2020 and 2069.

A number of uncertainties affect the calculation of the provision including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. The provision incorporates our best estimate of the financial effect of these uncertainties, but future material changes in any of the assumptions could materially impact on the calculation of the provision. See note 29 for analysis of the sensitivities associated with our estimate.

The undiscounted amount of the provision at 31 March 2020 was £51m (2019: £52m), being the undiscounted best estimate liability having regard to these uncertainties.

Other provisions

The other provisions consist of claims (whether covered by insurance or not) including employer liability claims, dilapidations and other provisions relating to the operation of our gas networks. Where amounts are material, third party valuations are performed. Any insurance proceeds are recognised as an asset when virtually certain of recovery. The majority of claims are expected to be settled within 10 years.

24 Share capital

	2020 £m	2019 £m
Allotted, called up and fully paid		
5,105,581,781 ordinary shares of £0.0001 each	**1**	1

Each share carries the right to one vote on a poll. The right to vote is determined by reference to the register of members. All dividends shall be declared and paid according to the amounts paid up on the shares. The shares do not carry any rights as respects to capital to participate in a distribution (including on a winding-up) other than those that exist as a matter of law. The shares are not redeemable.

25 Net debt

Net debt is a measure which shows the overall debt situation. Net debt is calculated by netting the value of a company's liabilities and debts with its cash and other similar short-term financial assets.

	2020 £m	2019 £m
Increase/(decrease) in cash and cash equivalents	**15**	(12)
(Decrease)/increase in financial investments	**(7)**	178
Increase in borrowings & related derivatives*	**(298)**	(345)
Repayment of lease liabilities*	**7**	-
Net interest paid on components of net debt	**232**	207
Change in net debt arising from cash flows	**(51)**	28
Changes in fair value of financial assets and liabilities and exchange movements	**(24)**	(9)
Other non-cash changes	**(28)**	-
Net interest charge on the components of net debt	**(279)**	(264)
Movement in net debt (net of related derivative financial instruments)	**(382)**	(245)
Net debt (net of related derivative financial instruments) at the start of the period	**(9,221)**	(8,976)
Net debt (net of related derivative financial instruments) at the end of the period	**(9,603)**	(9,221)

Composition of net debt:

	2020 £m	2019 £m
Cash, cash equivalents and financial investments	**358**	351
Borrowings and bank overdrafts	**(9,905)**	(9,542)
Derivatives	**(29)**	(30)
Lease liabilities	**(27)**	-
Total net debt	**(9,603)**	(9,221)

*In 2018/19 borrowings includes movements in relation to finance leases under IAS 17. In 2019/20 movements in lease liabilities relate to those recognised under IFRS 16 'Leases'. For details of amounts recognised on adoption of IFRS 16, see notes 1(c) and 22.

Notes to the consolidated financial statements (continued)
For the year ended 31 March 2020

25 Net debt (continued)

Analysis of changes in net debt:

	Cash and cash equiva-lents £m	Bank Overdrafts £m	Net cash and cash equiva-lents £m	Financial invest-ments £m	Borrow-ings £m	Deriva-tives £m	Lease Liabilities £m	Total £m
Cost								
At 1 April 2019	12	(9)	3	339	(9,533)	(30)	-	(9,221)
Adoption of IFRS 16	-	-	-	-	6	-	(29)	(23)
At 1 April 2019 (restated)	**12**	**(9)**	**3**	**339**	**(9,527)**	**(30)**	**(29)**	**(9,244)**
Cash flow	14	1	15	(7)	(60)	(6)	7	(51)
Fair value gains and losses and exchange movements	-	-	-	-	(36)	12	-	(24)
Interest charges	-	-	-	-	(274)	(5)	-	(279)
Other non-cash changes	-	-	-	-	-	-	(5)	(5)
At 31 March 2020	**26**	**(8)**	**18**	**332**	**(9,897)**	**(29)**	**(27)**	**(9,603)**

Balances at 31 March 2020 comprise:

Non-current assets	-	-	-	-	-	44	-	44
Current assets	26	-	26	332	-	-	-	358
Current liabilities	-	(8)	(8)	-	(131)	-	(9)	(148)
Non-current liabilities	-	-	-	-	(9,766)	(73)	(18)	(9,857)
At 31 March 2020	**26**	**(8)**	**18**	**332**	**(9,897)**	**(29)**	**(27)**	**(9,603)**

	Cash and cash equiva-lents £m	Bank Overdrafts £m	Net cash and cash equiva-lents £m	Financial invest-ments £m	Borrow-ings £m	Deriva-tives £m	Total £m
Cost							
At 1 April 2018	20	(5)	15	161	(9,158)	6	(8,976)
Cash flow	(8)	(4)	(12)	178	(136)	(2)	28
Fair value gains and losses and exchange movements	-	-	-	-	16	(25)	(9)
Interest charges	-	-	-	-	(255)	(9)	(264)
Other non-cash changes	-	-	-	-	-	-	-
At 31 March 2019	12	(9)	3	339	(9,533)	(30)	(9,221)

25 Net debt (continued)

Balances at 31 March 2019 comprised:

	Cash and cash equiva-lents £m	Bank Overdrafts £m	Net cash and cash equiva-lents £m	Financial invest-ments £m	Borrow-ings £m	Deriva-tives £m	Total £m
Non-current assets	-	-	-	-	-	8	8
Current assets	12	-	12	339	-	-	351
Current liabilities	-	(9)	(9)	-	(57)	-	(66)
Non-current liabilities	-	-	-	-	(9,476)	(38)	(9,514)
At 31 March 2019	12	(9)	3	339	(9,533)	(30)	(9,221)

26 Capital and other commitments

	2020	2019
	£m	£m
Contracts for future capital expenditure not provided in the financial statements	**556**	387
Letters of credit	**300**	300
	856	687

27 Pensions

The Group operates a number of pension schemes for its employees.

Defined contribution ('DC') scheme

For DC pension plans, the Group pays contributions into separate funds on behalf of the employee and has no further obligations to employees. The risks associated with this type of plan are assumed by the member.

MyPension, the Group's DC arrangement, was established on 1 February 2019. Under the standard contribution structure, the Group double matches member contributions to MyPension up to a maximum of 6%. MyPension is the qualifying scheme used for automatic enrolment and new hires are enrolled into MyPension.

Prior to that, employees contributed to the National Grid YouPlan. At 31 August 2018 a bulk transfer of £85.5m was effected from YouPlan to MyPension and all DC benefits are now managed under MyPension.

The amount recognised as an expense for the defined contribution scheme was:

	2020	2019
	£ m	£ m
Current period contributions	**16**	15

Defined benefit ('DB') scheme

The Group's DB pension arrangements are held in the National Grid UK Pension Scheme (the Scheme). With effect from 1 January 2017 the Scheme was split into three sections, each of which is legally and actuarially separate. Section C is supported by the Group and active membership is limited to the Group's employees. Sections A and B are supported by companies within the National Grid Group.

Members receive benefits on retirement, the value of which is dependent on factors such as salary and length of pensionable service. The Group underwrites both financial and demographic risks associated with this type of scheme.

The cost of providing benefits in a DB scheme is determined using the projected unit method, with actuarial valuations being carried out at each reporting date by a qualified actuary. This valuation method is an accrued benefits valuation method that makes allowance for projected earnings.

The Group's obligation in respect of the Scheme is calculated separately for Section C of the Scheme by projecting the estimated amount of future benefit payments that employees have earned for their pensionable service in the current and prior periods. These future benefit payments are discounted to determine the present value of the liabilities and the fair value of plan assets and any unrecognised past service cost is then deducted. The discount rate used is the yield at the valuation date on high-quality corporate bonds.

The Group takes advice from independent actuaries relating to the appropriateness of any key assumptions applied which include life expectancy of members, expected salary and pension increases, and inflation. It should be noted that comparatively small changes in the assumptions used may have a significant effect on the amounts recognised in the income statement and the statement of other comprehensive income and the net asset recognised in the statement of financial position. For sensitivity analysis, see note 29.

27 Pensions (continued)

Remeasurements of net retirement obligations are recognised in full in the period in which they occur in the statement of other comprehensive income.

The Scheme is funded with assets held in a separate Trustee administered fund. The arrangements are managed by a Trustee company with a board consisting of company and member appointed directors. The Directors are required to manage the arrangements in accordance with local regulations and the arrangements' governing documents, acting on behalf of its beneficiaries.

The arrangements are subject to independent actuarial funding valuations at least every three years and following consultation and agreement with the company, the qualified actuary certifies 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.

The last full actuarial valuation for the Scheme was carried out at 31 March 2019. As part of this valuation, based on long-term financial assumptions, a contribution rate to meet future benefit accrual was agreed of 52.1% of pensionable earnings less any member contributions. In addition, the company makes payments to the Scheme to cover administration costs and the Pension Protection Fund levy.

The results of the 2019 valuation are shown below:

Last full actuarial valuation	**31 March 2019**	31 March 2017
Actuary	**Willis Towers Watson**	Willis Towers Watson
Market value of scheme assets at latest valuation	**£6,674**	£7,004
Actuarial value of benefits due to members	**£6,755**	£7,233
Market value as percentage of benefits	**99%**	97%
Funding deficit	**£81m**	£229m

The 2017 and 2019 valuations cover only Section C, which is supported by the Group.

Section C of the Scheme

The Group and the Trustees have agreed a schedule of contributions with payments of £22m per year during FY22 and FY23. Payments will be made quarterly from April 2021 with the final payment due by September 2022.

27 Pensions (continued)

Section C of the Scheme (continued)

The Group has established a security arrangement with a charge in favour of the Trustees. This amount may change over time or following changes to the operating company's credit rating or gearing levels. At 31 March 2020 the value of this was required to be £257m. This was provided via £300m in letters of credit. The assets held as security will be paid to Section C in the event that the company is subject to an insolvency event, if the operating company is given notice of less than 12 months that Ofgem intends to revoke its licence under the Gas Act 1986, if the Group fails to make the required contributions in relation to Section C, if the operating company's credit rating by two out of three specified agencies falls below certain agreed levels for a period of 40 days, or if the operating company grants any charges over its assets other than where agreed with the trustees. The assets held as security will be released back to the company if the Scheme moves into surplus. In addition, the operating company will make a further payment of £72m (increased in line with RPI) into Section C if the operating company's credit rating by two out of three specified agencies falls below certain agreed levels for a period of 40 days.

The Scheme ceased to allow new hires to join from 1 April 2002, with new hires since that date having the option of joining the DC arrangement.

Following the sale of National Grid's remaining stake in Cadent Gas Limited to the Group in June 2019, the Group has put in place its own DB pension arrangement, the Cadent Gas Pension Scheme, in order to request a transfer of the assets and liabilities of Section C into the scheme. A new corporate Trustee company was incorporated on 19 December 2019, Cadent Gas Pension Trustee Limited and two further holding companies 'Cadent Gas Pension Property Company 1 Limited' and 'Cadent Gas Pension Property Company 2 Limited' were incorporated on 25 March 2020. On 17 June 2020 a further company was incorporated 'Cadent Gas Pension Services Limited'. A bulk transfer is targeted during the 2020/21 financial year. All costs associated with the creation of this new scheme have been treated as an exceptional item.

Risks

The DB pension obligations and other post-retirement benefit liabilities are exposed to the primary risks outlined below.

Liabilities are calculated using discount rates set with reference to yields on high-quality corporate bonds prevailing in the UK debt markets and will fluctuate as yields change. Scheme funds are invested in a variety of asset classes, principally: equities, government securities, corporate bonds and property. Consequently, actual returns will differ from the underlying discount rate adopted and therefore have an impact on the net balance sheet liability.

Changes in inflation will affect both current and future pension payments and are partially mitigated through investment in inflation matching assets and hedging instruments.

The Chancellor's announcement on 4 September 2019 on the future of the RPI makes it likely that RPI will be aligned with CPIH from 2030 if not earlier. The market response to the announcement created uncertainty about the extent to which this potential change is priced into breakeven inflation rates implied by the gilt markets. Historically, CPIH inflation has been around 1% lower than RPI inflation but the reduction in long-term market estimates of RPI inflation as a result of the announcement was much smaller than expected. In prior years, the RPI inflation assumption adopted was based on market implied RPI inflation less an inflation risk premium adjustment of 0.2% per annum. Due to the uncertainty in the market, this inflation risk premium adjustment has been increased to 0.3% per annum in FY20 to allow for some but not all the expectation that RPI inflation will be lower in the future.

27 Pensions (continued)

Risks (continued)

Longevity is also a key driver of liabilities and changes in expected mortality will have a direct impact on liabilities. The liabilities are, in aggregate, relatively mature which serves to mitigate this risk to some extent.

Each scheme's investment strategy seeks to balance the level of investment return sought with the aim of reducing volatility and risk. In undertaking this approach reference is made both to the maturity of the liabilities and the funding level of that plan. A number of further strategies are employed to manage underlying risks, including liability matching asset strategies, diversification of asset portfolios, interest rate hedging and management of foreign exchange exposure.

COVID-19, which has had a global impact since early 2020, has led to a deterioration in the asset valuations used in the IAS 19 assessment of the surplus position of Section C. In particular, it has resulted in an increased level of volatility in asset markets and a worsening in market conditions. In light of COVID-19 and the resulting impact on financial markets there is significant uncertainty over certain pension asset valuations, particularly of the property (£273m) and unquoted equities (£730m) portfolios as at 31 March 2020. A higher degree of caution has been attached to the property valuations received from external parties due to the unknown future impact that COVID-19 might have on the real estate market. For the property portfolio, our valuation reports from our surveyors are subject to material valuation uncertainty clauses as set out in the RICS guidance due to the impact COVID-19 has had on previous market evidence, however, we do not believe that this is likely to result in a material change in the value disclosed. For unquoted equities amounting to £54m where it was not possible to obtain valuations at 31 March 2020, a benchmark reduction based on market evidence was applied.

The recognition of the net defined benefit asset in relation to Section C of the Scheme reflects legal and actuarial advice that we have taken regarding recognition of surpluses under IFRIC 14. We have concluded that the Group has an unconditional right to a refund from the plan, in the event of a winding-up. The Trustees must seek the agreement of the Group to any benefit augmentation beyond the provisions set out in the Scheme Rules.

Amounts recognised in the statement of financial position

The following tables represent the amounts in the financial statements.

	2020 Total £m	2019 Total £m
Present value of funded obligations	**(5,572)**	(5,981)
Fair value of plan assets	**6,492**	6,674
	920	693
Present value of unfunded obligations	**(3)**	(3)
Net defined benefit asset	**917**	690

Represented by:	**2020 Total £m**	2019 Total £m
Liabilities	**(5,575)**	(5,984)
Assets	**6,492**	6,674
	917	690

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2020

27 Pensions (continued)

Amounts recognised in the income statement and statement of other comprehensive income

	2020 Total £m	2019 Total £m
Included within operating costs		
Administration costs	**4**	3
Defined contribution scheme costs	**16**	15
Defined benefit scheme costs:		
Current service cost	**16**	20
Past service costs (disclosed as an exceptional item)	**18**	14
	54	52
Included within finance costs		
Net interest credit	**(17)**	(14)
Total included in income statement	**37**	38
Remeasurements of net retirement benefit obligations	**(190)**	35
Return on plan assets greater or less than discount rate	**14**	(167)
Total included in the statement of other comprehensive income	**(176)**	(132)

Reconciliation of the net defined benefit asset

	2020 Total £m	2019 Total £m
Opening net defined benefit asset	**690**	507
Costs recognised in the income statement	**(21)**	(23)
Employer contributions	**72**	75
Other movements	**176**	131
Closing net defined benefit asset	**917**	690

Changes in the present value of defined benefit obligations (including unfunded obligations)

	2020 Total £m	2019 Total £m
Opening net defined benefit liability	**5,984**	6,309
Current service cost	**16**	20
Interest cost	**139**	156
Past service cost	**18**	14
Actuarial losses – experiences	**(40)**	38
Actuarial losses/(gains) – demographic assumptions	**189**	(259)
Actuarial (gains)/losses – financial assumptions	**(339)**	256
Benefits paid	**(392)**	(551)
Other	**-**	1
Closing net defined benefit liability	**5,575**	5,984

27 Pensions (continued)

Changes in the fair value of plan assets

	2020	2019
	Total	Total
	£m	£m
Opening fair value of plan assets	**6,674**	6,816
Interest income	**156**	170
Return on assets (less)/greater than assumed	**(14)**	167
Administration costs	**(4)**	(3)
Employer contributions paid	**72**	75
Benefits paid	**(392)**	(551)
Closing fair value of plan assets	**6,492**	6,674
Actual return on plan assets	**142**	337
Expected contributions to plans in the following year	**22**	80

Asset allocations

Within the asset allocations below there is significant diversification across regions, asset managers, currencies and bond categories.

	2020	**2020**	**2020**	**2019**	**2019**	**2019**
	Quoted	**Unquoted**	**Total**	**Quoted**	**Unquoted**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Equities	**507**	**226**	**733**	717	248	965
Corporate bonds	**2,088**	**-**	**2,088**	1,844	-	1,844
Property	**-**	**273**	**273**	-	363	363
Government securities	**2,742**	**-**	**2,742**	2,944	-	2,944
Diversified alternatives (i)	**-**	**504**	**504**	-	401	401
Other	**-**	**152**	**152**	-	157	157
Total	**5,337**	**1,155**	**6,492**	5,505	1,169	6,674

i) Includes return seeking non-conventional asset classes of £296m (2019: £312m), secure income assets of £208m (2019: £88m) and other of £Nil (2019: £1m).

The investment strategy for Section C of the Scheme is formulated specifically in order to manage risk, through investment in diversified asset classes, including the use of liability matching assets and where appropriate through the employment of interest rate and inflation hedging instruments. The asset allocation at 31 March 2020 is as follows:

	2020	2019
	%	%
Equities	**11**	15
Other	**89**	85
	100	100

27 Pensions (continued)

Actuarial assumptions

Cadent Gas Limited has applied the following financial assumptions in assessing defined benefit liabilities.

	2020	2019
	%	%
Discount rate – Past service (i)	**2.25**	2.40
Discount rate – Future service (i)	**2.20**	2.45
Rate of increase in salaries (ii)	**1.80**	3.50
Rate of increase in RPI – Past service (iii)	**2.55**	3.25
Rate of increase in RPI – Future service (iii)	**2.40**	3.20

i) The discount rate for pension liabilities has been determined by reference to appropriate yields on high quality corporate bonds prevailing in the UK debt market at the reporting date. Future and past discount rates are set based on the expected duration of scheme liabilities.

ii) A promotional scale has also been used where appropriate. The assumption stated is that relating to service prior to 1 April 2014. The assumption for the rate of increase in salaries for service after this date is 2.15% (2019: 2.20%).

iii) This is the key assumption that determines assumed increases in pensions in payment and deferment. Consistent with the derivation of the discount rate, the RPI assumption reflects the duration of the active liabilities to be adopted in the calculation of future service obligations.

For sensitivity analysis, see note 29.

Assumed life expectations for a retiree age 65.

	2020	2019
	years	years
Today		
Males	**21.3**	20.8
Females	**24.5**	22.8
In 20 years		
Males	**22.6**	22.1
Females	**25.9**	24.3

Maturity profile of DB obligations

The weighted average duration of the DB obligation for future service obligations of the scheme is 26 years and 16 years for past service obligations.

28 Financial risk management

Our activities expose us to a variety of financial risks including currency risk, interest rate risk, credit risk, capital risk and liquidity risk. Our risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential volatility of financial performance from these risks. We use financial instruments, including derivative financial instruments, to manage risks of this type.

This note describes our approach to managing risk, including an analysis of assets and liabilities by currency type and an analysis of interest rate category for our net debt. We are required by accounting standards to also include a number of specific disclosures, (such as a maturity analysis of contractual undiscounted cash flows) and have included these requirements below.

Risk management related to financing activities is carried out by a central treasury department under policies approved by the Finance Committee of the Board of its main operating company, Cadent Gas Limited. The objective of the treasury department is to manage funding and liquidity requirements, including managing associated financial risks, to within acceptable boundaries. The Finance Committee provides written principles for overall risk management, as well as written policies covering specific areas such as foreign exchange risk, interest rate risk, credit risk, liquidity risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity.

We have exposure to the following risks, which are described in more detail below:

- Credit risk;
- Liquidity risk;
- Interest rate risk;
- Currency risk; and
- Capital risk.

(a) Credit risk

Credit risk refers to the risk that a counterparty will default on their contractual obligations resulting in a financial loss to the Group. This risk is inherent in our commercial business activities. We are exposed to credit risk on our cash and cash equivalents, derivative financial instruments, deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables and committed transactions.

The Group has assessed whether there is any impact of COVID-19 on credit risk. The impact was deemed to be limited given the nature of the business in that our principal commercial exposure relates to shipper income which is governed by the credit rules within the Uniform Network Code. There are a number of actions the Group takes to mitigate any credit risk and changes to credit rules have been agreed across the gas industry with involvement from Ofgem.

The carrying amount of financial assets and loss allowance are as follows:

For the year ended 31 March 2020

	Notes	Gross carrying amount	Loss allowance	Net carrying amount
		£m	£m	£m
Cash and cash equivalents		**26**	**-**	**26**
Derivative financial assets	17	**44**	**-**	**44**
Trade debtors	16	**13**	**(3)**	**10**
Accrued income	16	**173**	**-**	**173**
Current asset investments	18	**332**	**-**	**332**

28 Financial risk management (continued)

(a) Credit risk (continued)

For the year ended 31 March 2019

	Notes	Gross carrying amount	Loss allowance	Net carrying amount
		£m	£m	£m
Cash and cash equivalents		12	-	12
Derivative financial assets	17	8	-	8
Receivables	16	19	(3)	16
Accrued income	16	166	-	166
Current asset investments	18	339	-	339

Counterparty credit risk
Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments. Our limits are managed by the central treasury department of the Group.

As at 31 March 2020, we had exposure to various financial institutions. In accordance with our treasury policies, counterparty credit exposure utilisations are monitored daily against the counterparty credit limits. Counterparty credit ratings and market conditions are reviewed continually with limits being revised and utilisation adjusted, if appropriate. Derivative financial assets are only entered into with banks with a strong Investment Grade Credit rating, which should reduce the likelihood of significant losses. Management does not expect any significant losses from non performance by these counterparties.

Customer credit risk
The Group's principal commercial exposure relates to income from shippers which is governed by the credit rules within the Uniform Network Code. These set out the level of credit relative to the RAV for each credit rating. The Group minimises customer credit risk by ensuring all customers can adequately demonstrate the ability to pay debts as they fall due. These include company credit rating, letter of credit from a financial institution, parent company guarantee, independent assessment, payment history allowance and advanced cash deposits.

	2020 Total	2019 Total
	£m	£m
Accrued income	**173**	166
Collateral held	**(33)**	(17)
Exposure net of collateral	**140**	149

Collection activities are monitored on a daily basis and late payment will result in sanctions being placed on the relevant accounts. The utilisation of credit limits is regularly monitored and collateral is collected against these accounts when necessary. Management does not expect any significant losses of receivables that have not been provided for as shown in note 16.

28 Financial risk management (continued)

(a) Credit risk (continued)

Offsetting financial assets and liabilities

The following tables set out financial assets and liabilities which are subject to offset and to enforceable master netting arrangements or similar agreements. The tables show the amounts which are offset and reported net in the statement of financial position. Amounts which cannot be offset under IFRS, but which could be settled net under terms of master netting agreements if certain conditions arise, and with collateral received or pledged, are shown to present Quadgas MidCo's net exposure.

Financial assets and liabilities on different transactions are only reported net if the transactions are with the same counterparty, a legal right of offset exists and the cash flows are intended to be settled on a net basis.

Amounts which do not meet the criteria for offsetting on the statement of financial position but could be settled net in certain circumstances principally relate to derivative transactions under ISDA (International Swaps and Derivatives Association) agreements where each party has the option to settle amounts on a net basis in the event of default of the other party.

Quadgas MidCo has similar arrangements in relation to bank account balances and bank overdrafts; and trade payables and trade receivables which are subject to general terms and conditions. However, these balances are immaterial.

	Gross carrying amounts	Gross amounts offset	Net amount presented in statement of financial position	Financial instruments	Cash collateral received/ pledged	Net amount
At 31 March 2020	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Assets						
Derivatives financial instruments	**44**	**-**	**44**	**-**	**-**	**44**
Liabilities						
Derivatives financial instruments	**(73)**	**-**	**(73)**	**-**	**-**	**(73)**
Total at 31 March 2020	**(29)**	**-**	**(29)**	**-**	**-**	**(29)**

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2020

28 Financial risk management (continued)

(a) Credit risk (continued)

	Gross carrying amounts	Gross amounts offset	Net amount presented in statement of financial position	Financial instruments	Cash collateral received/ pledged	Net amount
At 31 March 2019	£m	£m	£m	£m	£m	£m
Assets						
Derivatives financial instruments	8	-	8	-	-	8
Liabilities						
Derivatives financial instruments	(38)	-	(38)	-	-	(38)
Total at 31 March 2019	(30)	-	(30)	-	-	(30)

(b) Liquidity risk

We determine our liquidity requirements by the use of both short-term and long-term cash flow forecasts. These forecasts are supplemented by a financial headroom analysis which is used to assess funding adequacy for at least a 12 month period and maintain adequate liquidity for a continuous 12 month period.

We believe our contractual obligations, including those shown in capital and other commitments in note 26 can be met from existing cash and investments, operating cash flows and internal or external financing that we reasonably expect to be able to secure in the future, together with the use of committed facilities if required.

Our debt agreements and banking facilities contain covenants, including those relating to the periodic and timely provision of financial information by the issuing entity, and financial covenants such as maintaining current rating levels. Failure to comply with these covenants, or to obtain waivers of these requirements, could in some cases trigger a right, at the lender's discretion, to require repayment of some of our debt, and may restrict our ability to draw upon our facilities to access the capital markets.

The Group has assessed whether there is any impact of COVID-19 on its liquidity risk. Currently there has not been a significantly adverse impact on cash flows but the Group Treasury function continue to monitor this in line with forecasts for future requirements.

28 Financial risk management (continued)

(b) Liquidity risk (continued)

The following is an analysis of the contractual undiscounted cash flows payable under financial liabilities and derivative assets and liabilities as at the reporting date:

At 31 March 2020	**Due within 1 year £m**	**Due between 1 and 2 years £m**	**Due between 2 and 3 years £m**	**Due 3 years and beyond £m**	**Total £m**
Non-derivative financial instruments					
Borrowings	**(70)**	**(250)**	**-**	**(10,033)**	**(10,353)**
Lease Liabilities (i)	**(9)**	**(5)**	**(3)**	**(10)**	**(27)**
Interest on payments on borrowings (ii)	**(241)**	**(239)**	**(236)**	**(3,407)**	**(4,123)**
Other non-interest bearing liabilities	**(594)**	**-**	**-**	**-**	**(594)**
Derivative financial instruments					
Derivative contracts - receipts	**26**	**26**	**26**	**1,525**	**1,603**
Derivative contracts - payments	**(28)**	**(28)**	**(28)**	**(1,624)**	**(1,708)**
Total at 31 March 2020	**(916)**	**(496)**	**(241)**	**(13,549)**	**(15,202)**

i) In the previous year, the group recognised finance lease liabilities under IAS 17 within borrowings. In the current year lease liabilities under IFRS 16 are included within lease liabilities.

ii) The interest on borrowings is calculated based on borrowings held at 31 March without taking account of future issues. Floating rate interest is estimated using a forward interest rate curve as at 31 March. Payments are included on the basis of the earliest date on which the company can be required to settle.

At 31 March 2019	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due 3 years and beyond £m	Total £m
Non-derivative financial instruments					
Borrowings	-	-	(1,264)	(9,207)	(10,471)
Interest on payments on borrowings (i)	(240)	(242)	(236)	(2,553)	(3,271)
Other non-interest bearing liabilities	(560)	-	-	-	(560)
Derivative financial instruments					
Derivative contracts - receipts	24	24	25	1,052	1,125
Derivative contracts - payments	(20)	(20)	(20)	(1,149)	(1,209)
Total at 31 March 2019	(796)	(238)	(1,495)	(11,857)	(14,386)

i) The interest on borrowings is calculated based on borrowings held at 31 March without taking account of future issues. Floating rate interest is estimated using a forward interest rate curve as at 31 March. Payments are included on the basis of the earliest date on which the company can be required to settle.

28 Financial risk management (continued)

(c) Interest rate risk

Interest rate risk arises from our long-term borrowings. Borrowings issued at variable rates expose us to cash flow interest rate risk, partially offset by cash held at variable rates. Borrowings issued at fixed rates expose us to fair value interest rate risk.

Our interest rate risk management policy is to seek to minimise total financing costs (being interest costs and changes in the market value of debt) subject to constraints. We do this by using fixed and floating rate debt and derivative financial instruments including interest rate swaps, swaptions and forward rate agreements.

We hold some borrowings on issue that are inflation linked. We believe that these provide a partial economic offset to the inflation risk associated with our UK inflation linked revenues.

The table in note 21 (Borrowings) sets out the carrying amount, by contractual maturity, of borrowings that are exposed to interest rate risk before taking into account interest rate swaps.

During 2020, net debt was managed using derivative instruments to hedge interest rate risk as follows:

As at 31 March 2020	**Fixed rate £m**	**Floating rate £m**	**RPI £m**	**Other (i) £m**	**Total £m**
Borrowings	**(7,044)**	**(1,077)**	**(1,784)**	**-**	**(9,905)**
Financial investments (i)	**-**	**358**	**-**	**-**	**358**
Lease Liabilities (ii)	**-**	**-**	**-**	**(27)**	**(27)**
Pre-derivative position	**(7,044)**	**(719)**	**(1,784)**	**(27)**	**(9,574)**
Derivative effect	**30**	**400**	**(459)**	**-**	**(29)**
Net debt position (iii)	**(7,014)**	**(319)**	**(2,243)**	**(27)**	**(9,603)**

i) Represents financial instruments which are not directly affected by interest rate risk, including investments in equity or other non-interest bearing instruments.

(ii) In the previous year, the group recognised finance lease liabilities under IAS 17 within borrowings. In the current year lease liabilities under IFRS 16 are included within lease liabilities.

(iii) The impact of 2019/20 short-dated interest rate derivatives is included.

During 2019, net debt was managed using derivative instruments to hedge interest rate risk as follows:

As at 31 March 2019	Fixed rate £m	Floating rate £m	RPI £m	Other (i) £m	Total £m
Borrowings	(6,675)	(1,095)	(1,766)	(6)	(9,542)
Financial investments (i)	-	351	-	-	351
Pre-derivative position	(6,675)	(744)	(1,766)	(6)	(9,191)
Derivative effect	5	400	(435)	-	(30)
Net debt position (ii)	(6,670)	(344)	(2,201)	(6)	(9,221)

i) Represents financial instruments which are not directly affected by interest rate risk, including investments in equity or other non-interest bearing instruments.

ii) The impact of 2018/19 short-dated interest rate derivatives is included.

28 Financial risk management (continued)

(d) Currency risk

We are exposed to foreign exchange risk arising from non-sterling future commercial transactions and non-sterling recognised assets and liabilities.

Our policy for managing foreign exchange risk is to hedge contractually committed foreign currency cash flows over a prescribed minimum size. Where foreign currency cash forecasts are less certain, our policy is to hedge a proportion of the cash flows based on the probability of those cash flows occurring. Instruments used to manage foreign exchange transaction risk include foreign exchange forward contracts and foreign exchange swaps.

During 2020, derivative financial instruments were used to manage foreign currency risk as follows:

As at 31 March 2020	**Sterling £m**	**Euro £m**	**Japanese Yen £m**	**Dollar £m**	**Total £m**
Financial investments	**358**	**-**	**-**	**-**	**358**
Borrowings	**(8,536)**	**(1,092)**	**(76)**	**(201)**	**(9,905)**
Lease Liabilities (i)	**(27)**	**-**	**-**	**-**	**(27)**
Pre-derivative position	**(8,205)**	**(1,092)**	**(76)**	**(201)**	**(9,574)**
Derivative effect	**(1,398)**	**1,092**	**76**	**201**	**(29)**
Net debt position	**(9,603)**	**-**	**-**	**-**	**(9,603)**

i) In the previous year, the group recognised finance lease liabilities under IAS 17 within borrowings. In the current year lease liabilities under IFRS 16 are included within lease liabilities.

During 2019, derivative financial instruments were used to manage foreign currency risk as follows:

As at 31 March 2019	Sterling £m	Euro £m	Japanese Yen £m	Dollar £m	Total £m
Financial investments	351	-	-	-	351
Borrowings	(8,644)	(636)	(69)	(193)	(9,542)
Pre-derivative position	(8,293)	(636)	(69)	(193)	(9,191)
Derivative effect	(928)	636	69	193	(30)
Net debt position	(9,221)	-	-	-	(9,221)

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2020

28 Financial risk management (continued)

(d) Currency risk (continued)

Effect of hedge accounting on the financial position and performance

a) The impact of hedging instruments designated in a hedge relationship as at 31 March 2020 are as follows:

	Notional amount (GBP m)	**Carrying amount of the hedging instrument**		**Fair value changes**	**Line item in consolidated statement of financial position where hedging instrument is reported**
		Assets	**Liabilities**		
Cash flow hedges					
Cross-currency interest rate swaps	**1,337**	**44**	**(14)**	**25**	Derivative financial assets Derivative financial liabilities

The impact of hedging instruments designated in a hedge relationship as at 31 March 2019 were as follows:

	Notional amount (GBP m)	Carrying amount of the hedging instrument		Fair value changes	Line item in consolidated statement of financial position where hedging instrument is reported
		Assets	Liabilities		
Cash flow hedges					
Cross-currency interest rate swaps	895	8	(3)	(7)	Derivative financial assets Derivative financial liabilities

Notes to the consolidated financial statements (continued)

For the year ended 31 March 2020

28 Financial risk management (continued)

b) The impact of hedged items designated in a hedge relationship as at 31st March 2020 were as follows:

	Carrying amount of the hedged item (GBP m)		Fair value	Line item in consolidated statement of financial position where hedging	Cash flow hedge	Cost of hedging
	Assets	**Liabilities**	**changes**	**instrument is reported**	**reserve**	**reserve**
Cash flow hedges						
Non GBP denominated debt	**-**	**(1,369)**	**(36)**	Borrowings	**(6)**	**-**

The impact of hedged items designated in a hedge relationship as at 31st March 2019 were as follows:

	Carrying amount of the hedged item (GBP m)		Fair value	Line item in consolidated statement of financial position where hedging	Cash flow hedge	Cost of hedging
	Assets	Liabilities	changes	instrument is reported	reserve	reserve
Cash flow hedges						
Non GBP denominated debt	-	(898)	5	Borrowings	8	(1)

c) The impact of the hedging relationships on the consolidated income statement and other comprehensive income.

The above hedging relationships affected the consolidated income statements for year ended March 2020 are as follows:

	Change in value of hedging instrument recognised in OCI	Hedge ineffectiveness recognised in consolidated income statement	Line item in consolidated income statement where the hedge ineffectiveness is reported	Amount reclassified from cash flow hedge reserve to consolidated income statement	Line item in the consolid-ated income statement
Cash flow hedges					
Interest rate risk & FX risk	**(13)**	**1**	Exceptional items and remeasurements	**36**	Finance costs

The above hedging relationships affected the consolidated income statements for year ended March 2019 are as follows:

	Change in value of hedging instrument recognised in OCI	Hedge ineffectiveness recognised in consolidated income statement	Line item in consolidated income statement where the hedge ineffectiveness is reported	Amount reclassified from cash flow hedge reserve to consolidated income statement	Line item in the consolid-ated income statement
Cash flow hedges					
Interest rate risk & FX risk	(5)	4	Exceptional items and remeasurements	(9)	Finance costs

28 Financial risk management (continued)

(e) Capital risk management

The capital structure of the Group consists of shareholders' equity, as disclosed in the consolidated statement of changes in equity, and net debt (note 25). Our objectives when managing capital are: to safeguard our ability to continue as a going concern, to remain within regulatory constraints of our regulated operating company and to maintain an efficient mix of debt and equity funding thus achieving an optimal capital structure and cost of capital. We regularly review and manage the capital structure as appropriate in order to achieve these objectives.

Maintaining appropriate credit ratings for our main regulated operating company, Cadent Gas Limited, is an important aspect of our capital risk management strategy and balance sheet efficiency. We monitor our balance sheet efficiency by regulatory asset value (RAV) gearing calculated as adjusted net debt (statutory net debt adjusted for unamortised debt fees, unamortised fair value adjustments, accrued interest and derivatives) expressed as a percentage of RAV, which indicates the level of debt employed to fund our regulated business. It is compared with the level of RAV gearing indicated by Ofgem as being appropriate for our business, at around 62.5 - 65%. The RAV gearing ratio at the Cadent Gas Limited level was 31 March 2020 was 64% (2019: 62%).

(f) Fair value analysis

The financial instruments included in the statement of financial position are measured at fair value. These fair values can be categorised into hierarchy levels that are representative of the inputs used in measuring the fair value. The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used.

As at 31 March 2020	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Assets				
Fair value through profit and loss ('FVTPL') instruments	**358**	**-**	**-**	**358**
Derivative financial instruments	**-**	**44**	**-**	**44**
Liabilities				
Derivative financial instruments	**-**	**(73)**	**-**	**(73)**
Total	**358**	**(29)**	**-**	**329**

As at 31 March 2019	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**
Assets				
Fair value through profit and loss ('FVTPL') instruments	351	-	-	351
Derivative financial instruments	-	8	-	8
Liabilities				
Derivative financial instruments	-	(38)	-	(38)
Total	351	(30)	-	321

Level 1: Financial instruments with quoted prices for identical instruments in active markets.

Level 2: Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are based directly or indirectly on observable market data.

Level 3: Financial instruments valued using valuation techniques where one or more significant inputs are based on unobservable market data.

29 Sensitivity analysis

In order to give a clearer picture of the impact on our results or financial position of potential changes in significant estimates and assumptions, the following sensitivities are presented. These sensitivities are hypothetical, as they are based on assumptions and conditions prevailing at the period end, and should be used with caution. The effects provided are not necessarily indicative of the actual effects that would be experienced because our actual exposures are constantly changing.

The sensitivities in the table below show the potential impact in the income statement (and consequential impact on net assets) for a range of different variables each of which have been considered in isolation (i.e. with all other variables remaining constant). There are a number of these sensitivities which are mutually exclusive and therefore if one were to happen, another would not, meaning a total showing how sensitive our results are to these external factors is not meaningful.

We are further required to show additional sensitivity analysis for changes in interest and exchange rates and these are shown separately in the subsequent table due to the additional assumptions that are made in order to produce meaningful sensitivity disclosures.

The sensitivities included in the table below all have an equal and opposite effect if the sensitivity increases or decreases by the same amount unless otherwise stated. For example a 10% increase in unbilled revenue at 31 March 2020 would result in an increase in the income statement of £10 million and a 10% decrease in unbilled revenue would have the equal but opposite effect, except for goodwill impairment as previous impairments cannot be reversed.

	2020		2019	
	Income statement £m	**Net assets £m**	Income statement £m	Net assets £m
One year average increase in useful economic lives (pre-tax)				
Depreciation charge on property, plant and equipment	**16**	**16**	14	14
Amortisation charge on intangible assets	**3**	**3**	5	5
Environmental provision change in discount rate of 0.5%	**5**	**5**	5	5
Environmental provision change in undiscounted cash flow of 10%	**4**	**4**	4	4
Employer liability claims change in discount rate of 0.5%	**1**	**1**	1	1
Assets and liabilities carried at fair value change of 10% (pre-tax)				
Derivative financial instruments (i)	**3**	**3**	3	3
Goodwill impairment				
CPI change of 0.5%	**1,207**	**1,207**	726	726
Pre-tax discount rate change of 0.5%	**1,087**	**1,087**	874	874
Terminal value change of 0.05 multiple	**272**	**272**	159	159
Cost of Equity within Regulatory WACC – 0.5%	**386**	**386**	316	316
Pensions and other post-retirement benefits (ii) (pre-tax)				
Discount rate change of 0.5% (iii)	**2**	**417**	2	415
RPI rate change of 0.5% (iv)	**2**	**359**	2	397
Long-term rate of increase in salaries change of 0.5%	**-**	**34**	-	14
Change of one year to life expectancy at age 65	**1**	**227**	1	261
Change in value of unquoted properties by 5%	**-**	**14**	-	18
Change in value of unquoted equities by 5%	**-**	**37**	-	32
No hedge accounting for our derivative financial instruments (post tax)	**14**	**14**	6	6

29 Sensitivity analysis (continued)

i) The effect of a 10% change in fair value assumes no hedge accounting.
ii) The changes shown are a change in the annual pension or other post-retirement benefit service charge and change in the defined benefit obligations.
iii) A change in the discount is likely to occur as a result of changes in bond yields and as such would be expected to be offset to a significant degree by a change in the value of the bond assets held by the plans.
iv) The projected impact resulting from a change in RPI reflects the underlying effect on pensions in payment, pensions in deferment and resultant increases in salary assumptions.

	2020		2019	
	Income statement £m	**Net assets £m**	Income statement £m	Net assets £m
Financial risk (post-tax)				
UK RPI rate change of 0.5%	**9**	**9**	9	9
UK interest rate change of 0.5%	**4**	**4**	3	3

Financial instruments assumptions

Our financial instruments are sensitive to changes in market variables, being UK interest rates and the UK RPI. The changes in market variables impacts the valuation of our borrowings, deposits and derivative financial instruments. The analysis illustrates the sensitivity of our financial instruments to the changes in market variables.

The following main assumptions were made in calculating the sensitivity analysis:

• the amount of net debt, the ratio of fixed to floating interest rates of the debt and derivatives portfolio and the proportion of financial instruments in foreign currencies are all constant and on the basis of the hedge designations in place at 31 March 2020;

• the statement of financial position sensitivity to interest rates relates only to derivative financial instruments and FVTPL investments, as debt and other deposits are carried at amortised cost and so their carrying value does not change as interest rates move;

• the sensitivity of accrued interest to movements in interest rates is calculated on net floating rate exposures on debt, deposits and derivative instruments; and

• changes in the carrying value of derivatives from movements in interest rates of designated cash flow hedges are assumed to be recorded fully within equity.

30 Contingent liabilities

(a) Environmental claims

The environmental provision (see note 23) has been set up to deal with the costs of statutory decontamination of Cadent Gas Limited's UK old gas-manufacturing sites. Other claims have arisen from time to time, however none of these have been significant. It is not possible to determine the level of such future claims however, based upon experience, the Directors do not consider a provision necessary.

(b) Litigation

Through the ordinary course of operations, the company is party to various litigation, claims and investigations. The Directors do not expect the ultimate resolution of any of these proceedings to have a material adverse effect on the company's results of operations, cash flows or financial position.

(c) Guarantees and letters of credit

Group undertakings have entered into bonds and guarantees in the normal course of business. No liability is expected to arise in respect of bonds, guarantees or letters of credit.

31 Related Party Transactions

A related party is a company or individual who also has an interest in us. The related parties identified include fellow subsidiaries, joint ventures, associated undertakings, investments and key management personnel.

On 27 June 2019, National Grid Plc exercised the options over the further 14% interest in Quadgas HoldCo Limited (an indirect parent company of Quadgas MidCo Limited) and on 28 June 2019, National Grid Plc exercised the options over the remaining 25% interest in Quadgas HoldCo Limited. Post completion, 100% of the share capital in Quadgas HoldCo Limited is now owned by the consortium company Quadgas Investments BidCo Limited.

During the period ended 27 June 2019 the Group recorded £15m of income from National Grid Plc, and £42m of expenditure. At the balance sheet date of 31 March 2020 National Grid Plc are no longer considered a related party. There are nil balances outstanding with National Grid Plc in the table below.

	2020	2019
	£m	£m
Income:		
Goods and services supplied to associates	**-**	1
Goods and services supplied to other related parties	**15**	45
	15	46
Expenditure:		
Services rendered from associates	**10**	12
Services rendered from other related parties	**42**	202
Corporate services received	**-**	5
	52	219
Outstanding balances at 31 March in respect of income and expenditure:		
Amounts receivable from associates	**-**	-
Amounts receivable from other related parties	**-**	8
Amounts payable to associates	**1**	1
Amounts payable to other related parties	**-**	26

31 Related Party Transactions (continued)

Related party transactions were made on terms equivalent to those that prevail in arm's length transactions. Amounts receivable from or payable to related parties in respect of sales and expenditure are ordinarily settled one month in arrears. The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received.

Amounts of £Nil have been provided at 31 March 2020 and recognised as an expense (2019: £Nil) during the year in respect of bad or doubtful debts for related party transactions.

Details of key management compensation are provided in note 7.

32 Subsequent events

There are no post balance sheet events.

33 Ultimate parent company

The ultimate parent and controlling company is Quadgas Holdings TopCo Limited and the immediate parent company is Quadgas PledgeCo Limited. The largest and smallest group which includes the company and for which consolidated financial statements are prepared are headed by Quadgas Holdings TopCo Limited and Quadgas HoldCo Limited respectively. Quadgas Holdings TopCo Limited is registered in Jersey and Quadgas HoldCo Limited is registered in England and Wales.

Copies of Quadgas HoldCo Limited's consolidated financial statements can be obtained from the Company Secretary, Quadgas HoldCo Limited, Ashbrook Court, Prologis Park, Coventry, CV7 8PE.

Copies of Quadgas Holdings TopCo Limited's consolidated financial statements can be obtained from the Company Secretary, Quadgas Holdings TopCo Limited, 3rd Floor 37 Esplanade, St. Helier, Jersey, JE1 1AD.

34 Subsidiary undertakings

The list below contains all subsidiaries included within the Quadgas MidCo Group.

Name of subsidiary	% Holding	Principal activity	Country of incorporation
Cadent Gas Limited	100	Gas Distribution	England and Wales
Cadent Finance Plc	100*	Provision of long-term finance	England and Wales
Cadent Services Limited	100	Provision of services (including property management)	England and Wales
Quadgas Finance Plc	100	Provision of long-term finance	England and Wales
Cadent Gas Pension Trustee Limited	100*	Trustee of occupational pension scheme	England and Wales
Cadent Gas Pension Property Company 1 Limited	100*	Trustee of property assets of occupational pension scheme	England and Wales
Cadent Gas Pension Property Company 2 Limited	100*	Trustee of property assets of occupational pension scheme	England and Wales
Cadent Gas Pension Services Limited	100*	Management of pension services	England and Wales

The registered address for all subsidiaries is Ashbrook Court, Prologis Park, Coventry, CV7 8PE.

* Indirect holding

Quadgas MidCo Limited

Company statement of financial position
As at 31 March 2020

	Notes	2020 £m	2019 £m
Non-current assets			
Investments	6	**6,083**	6,296
Derivative financial assets	8	**4**	-
Total non-current assets		**6,087**	6,296
Current assets			
Trade and other receivables	7	**26**	40
Cash and cash equivalents		**7**	7
Current asset investments	9	**5**	7
Total current assets		**38**	54
Total assets		**6,125**	6,350
Current liabilities			
Borrowings	12	**(74)**	(2)
Trade and other payables	10	**(13)**	(12)
Total current liabilities		**(87)**	(14)
Non-current liabilities			
Borrowings	12	**(910)**	(898)
Trade and other payables	11	**(1,873)**	(1,872)
Total non-current liabilities		**(2,783)**	(2,770)
Total liabilities		**(2,870)**	(2,784)
Net assets		**3,255**	3,566
Equity			
Share capital	13	**1**	1
Retained earnings		**3,253**	3,566
Cash flow hedge reserve		**1**	(1)
Cost of hedging reserve		**-**	-
Total equity		**3,255**	3,566

The company has elected to take the exemption under Section 408 of the Companies Act 2006 from preparing the parent company profit and loss account. The loss for the year of £38m is disclosed in the statement of changes in equity.

The notes on pages 109 to 120 are an integral part of the financial statements.

The financial statements on pages 107 to 120 were approved by the Board of Directors on 12 August 2020 and signed on its behalf by:

M W Braithwaite
Director, Quadgas MidCo Limited
Company registration number: 10615396

Quadgas MidCo Limited

Company statement of changes in equity
For the year ended 31 March 2020

	Share capital £m	**Cash flow hedge reserve £m**	**Cost of hedging reserve £m**	**Retained earnings £m**	**Total £m**
At 1 April 2019	**1**	**(1)**	**-**	**3,566**	**3,566**
Loss for the year	**-**	**-**	**-**	**(38)**	**(38)**
Other comprehensive income for the year	**-**	**2**	**-**	**-**	**2**
Total comprehensive income for the year	**-**	**2**	**-**	**(38)**	**(36)**
Equity dividend	**-**	**-**		**(275)**	**(275)**
At 31 March 2020	**1**	**1**	**-**	**3,253**	**3,255**

	Share capital £m	Cash flow hedge reserve £m	Cost of hedging reserve £m	Retained earnings £m	Total £m
At 1 April 2018	1	(1)	-	5,037	5,037
Loss for the year	-	-	-	(1,131)	(1,131)
Other comprehensive income for the year	-	-	-	-	-
Total comprehensive loss for the year	-	-	-	(1,131)	(1,131)
Equity dividend	-	-	-	(340)	(340)
At 31 March 2019	1	(1)	-	3,566	3,566

Notes to the company financial statements

For the year ended 31 March 2020

1 Summary of significant accounting policies

We are required to include the stand-alone balance sheet of our parent company, Quadgas MidCo Limited, under the Companies Act 2006, and the statement of changes in equity under Financial Reporting Standard 101, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 101"). The following disclosures provide additional information to the stakeholders.

Quadgas MidCo Limited is a private company and is incorporated and domiciled in the United Kingdom and is registered in England and Wales. The address of its registered office is Ashbrook Court, Prologis Park, Central Boulevard, Coventry, CV7 8PE.

The principal accounting policies applied in the preparation of these financial statements are set out as below. These policies have been consistently applied to the current period presented, unless otherwise stated.

(a) Basis of preparation

The financial statements for the company have been prepared on the going concern basis under the historical cost convention modified to include certain items at fair value. Items included in the financial statements are measured using the currency of the primary economic environment in which the company operates (the 'functional currency'). The financial statements are presented in pounds sterling which is also the company's functional currency.

The statement of financial position shows net liabilities of £3,255,000 at 31 March 2020 (2019: £3,566,000). The income statement shows a loss for the year ended 31 March 2020 of £38,000 (2019: loss of £1,131,000) driven by the impairment of the investment held in Cadent Gas Limited, which is a non-cash movement The company continues to receive dividend income from Cadent Gas Limited which continues to trade and operate as a going concern and as at 31 March 2020 was in a net asset position of £2,153,000,000, reported profit for the financial year of £482,000,000, and had access to an undrawn £500,000,000 liquidity facility. See Cadent Gas Limited Annual report and accounts for further details.

In early 2020, the spread of a COVID-19 caused huge change to daily life in the UK and across the world. By nature of its operating business, Quadgas MidCo Limited has not been significantly impacted and having made enquiries and reviewed management's assessment of the going concern assumption, the Directors consider it appropriate to prepare the financial statements on a going concern basis. The going concern basis presumes that the company has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements are signed. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

(i) Parent company financial statements

The company meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100) issued by the Financial Reporting Council.

The financial statements have therefore been prepared in accordance with FRS 101 (Financial Reporting Standard 101) 'Reduced Disclosure Framework' as issued by the Financial Reporting Council.

As permitted by FRS 101, the company has taken advantage of the disclosure exemptions available under that standard in relation to business combinations, non-current assets held for sale, financial instruments, capital management, presentation of a cash flow statement, standards not yet effective, impairment of assets and related party transactions.

Where relevant, equivalent disclosures have been presented in the Group accounts of Quadgas MidCo Limited.

The preparation of financial statements may require management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the reported amounts of turnover and expenses during the reporting period. Actual results could differ from these estimates.

1 Summary of significant accounting policies (continued)

(b) New IFRS accounting standards and interpretations
As noted above, the 2020 Annual Report and Financial Statements have been prepared under FRS 101. As a result, the new accounting standard under IFRS, namely, IFRS 16 'Leases' is applicable to reporting periods beginning on or after 1 January 2019, and has therefore been adopted by the company for the period commencing 1 April 2019. It should be noted, however, that IFRS 16 has no impact on the company as the company has no leases.

(c) Investments
Investments in Group undertakings are held at cost less accumulated impairment losses.

Impairment reviews are carried out if there is some indication that impairment may have occurred, or where otherwise required to ensure that investments are not carried above their estimated recoverable amounts. Impairments are recognised in the income statement, and, where material, are disclosed separately.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. Recoverable amount is defined as the higher of net realisable value or estimated value-in-use at the date the impairment review is undertaken. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Impairment reversals are recognised when, in management's opinion, the reversal is permanent.

(d) Impairment of fixed assets
Impairment reviews are carried out if there is some indication that impairment may have occurred, or where otherwise required to ensure that fixed assets are not carried above their estimated recoverable amounts. Impairments are recognised in the income statement, and, where material, are disclosed as exceptional. Impairment reversals are recognised when, in management's opinion, the reversal is permanent.

Impairments of fixed assets are calculated as the difference between the carrying value of the net assets of income generating units, including where appropriate, investments, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value-in-use at the date the impairment review is undertaken. Net realisable value represents the amount that can be generated through the sale of assets. value-in-use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit.

(e) Financial instruments

Initial recognition
Financial assets, liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into.

1 Summary of significant accounting policies (continued)

(e) Financial instruments (continued)

Initial recognition (continued)
Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

Classification and measurement
Financial instruments are classified at inception into one of the following categories which then determines the subsequent measurement methodology:

Financial assets are classified into one of the following three categories:

- financial assets at amortised cost; and
- financial assets at fair value through other comprehensive income (FVTOCI); and
- financial assets at fair value through profit or loss (FVTPL).

Financial liabilities are classified into one of the following two categories:
- financial liabilities at amortised cost; and
- financial liabilities at fair value through profit and loss (FVTPL).

Loans receivable are carried at amortised cost using the effective interest method less any allowance for estimated impairments. Impairments are calculated using the expected credit loss approach by calculating the probability of default and the estimated recoverable amount given default.

Borrowings, which include interest-bearing loans, are recorded at their initial fair value which normally reflects the proceeds received, net of direct issue costs less any repayments. Subsequently these are stated at amortised cost, using the effective interest method. Any difference between proceeds and the redemption value is recognised over the term of the borrowing in the income statement using the effective interest method.

Accretion on inflation linked borrowings is accounted for on an accrual basis to the income statement, and are added to the carrying value of the debt instrument to the extent that they are not settled in the period in which they arise.

Derivative financial instruments (‘derivatives’) are recorded at fair value. Where the fair value of a derivative is positive, it is carried as a derivative asset and where negative, as a liability.

Assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right of set off exists and the cash flows are intended to be settled on a net basis. Gains and losses arising from changes in fair value are included in the income statement in the period they arise, unless hedge accounting applies.

The fair value of financial derivatives is calculated by discounting all future cash flows by the market yield curve at the reporting date and adjusting for own and counterparty credit. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates.

1 Summary of significant accounting policies (continued)

(e) Financial instruments (continued)

Classification and measurement (continued)
For financial assets carried at amortised cost, the amount of the impairment is the differences 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.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

Derecognition
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. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

Impairment of financial assets
The Group recognises loss allowances for expected credit losses (ECL) on financial instruments that are not measured at FVTPL, namely:

- trade receivables; and
- loan receivables; and
- other receivables.

The company measures the loss allowances on financial instruments at an amount equal to the 12 month expected credit loss (representing a stage 1 financial model). The way this is calculated is based on the applied impairment methodology, as described below:

Stage 1: For financial assets where there has not been a significant increase in credit risk since initial recognition, and were not credit impaired on recognition, the Group recognises a loss allowance based on the 12 month expected credit loss.

Stage 2: For financial assets where there has been a significant increase in credit risk since initial recognition, and were not credit impaired, the Group recognises a loss allowance for lifetime expected credit loss.

Stage 3: For financial assets which are credit impaired, the Group recognises the lifetime expected credit loss.

1 Summary of significant accounting policies (continued)

(e) Financial instruments (continued)

Impairment of financial assets (continued)
A significant increase in credit risk as a result of any change in circumstances specific to the counterparty or to the wider economic environment whereby the risk of default could be said to have been significantly increased within reasonable thresholds.

Evidence that the financial asset is credit impaired includes the following:
- significant financial difficulties of the counterparty; or
- a breach of contract such as default or past due event; or
- the restructuring of the loan or advance by the Group that the Group would not consider otherwise; or
- it is probably that the counterparty will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for an associated security because of financial difficulties.

(f) Trade and other receivables
Trade receivables are amounts due from customers for goods sold or services performed in the ordinary course of business. Trade receivables are initially recognised at the transaction price and are subsequently measured at amortised cost less a loss allowance.

(g) Trade and other payables
Trade payables are initially recognised at amortised cost and subsequently measured at amortised cost. Due to their short maturities, the fair value of trade and other payables approximates their book values.

(h) Tax
Current tax for the current period is provided at the amount expected to be paid or recovered from the tax authorities using the tax rates and tax laws enacted or substantively enacted by the reporting date.

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or the right to pay less tax, at a future date, at tax rates expected to apply when the timing differences reversed, based on tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements.

Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

(i) Dividends
Dividend income is recognised when the right to receive payment is established. Dividend distributions to the company's shareholders are recognised as a liability in the company's financial statements in the period in which the dividends are approved by the company's shareholders.

(j) Cash and cash equivalents
Cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position.

2 Critical accounting judgements and key sources of estimation uncertainty

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

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

Critical Accounting Judgements
Areas of judgement that have the most significant effect on the amounts recognised in the financial statements are as follows:

• Investments are reviewed annually for impairment by comparison of the cost of the investment with equity value, where equity value is equal to the value-in-use of the company invested in less any external borrowings plus any cash and cash equivalents - **note 6.**

Key Sources of Estimation Uncertainty
Key sources of estimation uncertainty that have significant risk of causing material adjustment to the carrying amounts of assets and liabilities in the next financial year are as follows:

• Review of carrying values of investments and calculation of impairment. The impairment review requires management to calculate the value-in-use for investments. The key assumptions for the value-in-use calculation are those regarding the underlying cash flows, discount rate, regulatory weighted average cost of capital, inflation and terminal value cash flow.

Notes to the company financial statements (continued)

For the year ended 31 March 2020

3 Auditor's remuneration

Auditor's remuneration in respect of the company is set out below:

	2020 £'000	2019 £'000
Audit services		
Audit fee of company	**74**	52
Other services		
Fees payable to the company's auditor for audit-related assurance services	**30**	29

4 Number of employees, including Directors

The average number of persons (including Executive Directors) employed by the company was Nil (2019: Nil).

5 Key management compensation

Key management comprises the Board of Directors of the company who have managerial responsibility for Cadent Gas Limited. Details of key management personnel compensation are provided in note 7 to the consolidated financial statements.

6 Investments

Shares in subsidiary undertakings	2020 £m	2019 £m
Cost		
At 1 April	**7,747**	7,747
Additions	**-**	-
At 31 March	**7,747**	7,747
Provision		
At 1 April	**(1,451)**	-
Impairment	**(213)**	(1,451)
At 31 March	**(1,664)**	(1,451)
Net book value at 31 March	**6,083**	6,296

The net carrying value of the investment held in Cadent Gas Limited, Cadent Services Limited and Quadgas Finance Plc was compared to its recoverable amount as part of the annual impairment review carried out by management.

The recoverable amount of the cash generating unit was determined from value-in-use calculations. The key assumptions for the value-in-use calculation are those regarding the underlying cash flows, discount rate, inflation and terminal value cash flow (see note 12 of the Quadgas MidCo Group Consolidated Financial Statements for further information).

6 Investments (continued)

The impairment review was completed following receipt of the Ofgem Draft Determinations on 9 July 2020 as the RIIO-2 settlement has the potential to impact the future cash flows and recoverable amount. The Draft Determinations included a challenging draft set of proposals, indicating the possibility of a further impairment arising over and above the impairment booked in the prior year following the publication by Ofgem of the RIIO-2 Sector Specific Methodology. Additionally, management considered the potential impact of COVID-19, determining the impact as not material to longer-term value due to the nature of the protections provided by the regulatory operating model but noting that it poses some short-term risks. The value-in-use reduced as a result of lower return expectations.

This resulted in a subsequent impairment of the investment held by Quadgas MidCo Limited in subsidiaries of £213m (2019; £1,451m) which was recognised in the Statement of Comprehensive Income in the year.

Carrying value comprised the investment in subsidiary undertakings.

Name of subsidiary	**% Holding**	**Principal activity**	**Country of incorporation**
Cadent Gas Limited	100	Gas Distribution	England and Wales
Cadent Services Limited	100	Provision of services (including property management)	England and Wales
Quadgas Finance Plc	100	Provision of long-term finance	England and Wales
Cadent Finance Plc	100*	Provision of long-term finance	England and Wales
Cadent Gas Pension Trustee Limited	100*	Trustee of occupational pension scheme	England and Wales
Cadent Gas Pension Property Company 1 Limited	100*	Trustee of property assets of occupational pension scheme	England and Wales
Cadent Gas Pension Property Company 2 Limited	100*	Trustee of property assets of occupational pension scheme	England and Wales
Cadent Gas Pension Services Limited	100*	Management of pension services	England and Wales

* Indirect holding

The registered address of these invesments is Ashbrook Court, Prologis Park, Coventry, CV7 8PE.

7 Trade and other receivables

	2020	2019
	£m	£m
Amounts falling due within one year:		
Amounts owed by subsidiary undertakings	**25**	36
Other debtors	**1**	4
	26	40

Amounts owed by subsidiary undertakings are unsecured, interest free and repayable upon demand.

8 Derivative financial instruments

The fair values of derivative financial instruments are as follows:

	2020		
	Assets £m	**Liabilities £m**	**Total £m**
Amounts falling due after more than one year	**4**	**-**	**4**
	4	**-**	**4**

	2019		
	Assets £m	Liabilities £m	Total £m
Amounts falling due after more than one year	-	-	-
	-	-	-

For each class of derivative the notional contract amounts* are as follows:

	2020 £m	2019 £m
Cross-currency interest rate swaps	**38**	38
	38	38

*The notional contract amounts of derivatives indicate the gross nominal value of transactions outstanding at the reporting date.

9 Current asset investments

	2020 £m	2019 £m
Investment in short-term money funds	**5**	7
	5	7

10 Trade and other payables falling due in less than one year

	2020 £m	2019 £m
Amounts owed to subsidiary undertakings	**13**	12
	13	12

11 Trade and other payables falling due in greater than one year

Non-current liabilities	2020 £m	2019 £m
Amounts owed to immediate parent company	902	902
Amounts owed to subsidiary company	971	970
	1,873	1,872

Amounts due to immediate parent undertakings are unsecured, at an arm's length interest rate of 6.8% (2019: 6.8%) and repayable on 30/04/2042.

Amounts owed to subsidiary undertakings reflect external debt raised by Quadgas Finance Plc and passed on to Quadgas MidCo Limited. The amounts are usually passed on to Quadgas MidCo Limited on identical terms to the amount raised in Quadgas Finance Plc. The amounts are unsecured with interest payments to 2027.

12 Borrowings

	2020 £m	2019 £m
Amounts falling due within one year		
Bank loans	72	-
Bonds	2	2
	74	2
Amounts falling due after more than one year		
Bank loans	219	217
Bonds	691	681
	910	898

Total borrowings are repayable as follows:

	2020 £m	2019 £m
Less than 1 year	74	2
In 1-2 years	-	-
In 2-3 years	-	217
In 3-4 years	-	-
In 4-5 years	219	-
More than 5 years	691	681
	984	900

12 Borrowings (continued)

The notional amount of borrowings outstanding as at 31 March 2020 was £942m (2019: £870m), £981m (2019: £899m) including accretion.

The company's borrowings comprise fixed rate, floating rate and indexed linked debt which has been issued out of the company. The table below summarises the debt, including their fair values.

Summary of Borrowings

Currency	Type	Notional* £m	Rate	Maturity Date	Interest £m	Book value £m	Fair Value £m
Fixed Rate							
GBP	Listed	125	Fixed	31/03/2037	1	125	130
		125			**1**	**125**	**130**
Index-linked							
GBP	Listed	286	RPI-linked	31/03/2042	-	284	263
GBP	Listed	43	RPI-linked	31/03/2037	-	42	42
GBP	Listed	80	RPI-linked	31/03/2042	-	82	70
GBP	Listed	80	RPI-linked	31/03/2037	-	82	76
		489			**-**	**490**	**451**
Floating Rate							
GBP	Listed	77	LIBOR +	31/03/2037	1	78	68
GBP	Unlisted	220	LIBOR +	11/07/2024	2	221	212
GBP	Listed	70	LIBOR +	18/06/2020	-	70	70
		367			**3**	**369**	**350**
Overdraft		**-**			**-**	**-**	**-**
TOTAL		**981**			**4**	**984**	**931**

* Index-linked debt notional is the accreted value

On 12 July 2019, Quadgas Midco Ltd refinanced its outstanding debt facilities extending the maturity to 2024 (previously 2022). This included repaying the existing syndicated term loan of £218m and drawing a new syndicated term loan of £220m. The undrawn Revolving Credit Facility of £200m was replaced with a new facility with a maturity date of 2024, as was the liquidity facility. The Group continues to have at its disposal sufficient undrawn, committed borrowing facilities at competitive rates for the medium term.

As of 31 March 2020, the fair value of all Quadgas MidCo Limited debt was £931m (2019: £903m). Where market values were available, the fair value of borrowings (Level 1) was £Nil (2019; £Nil). Where market values were not available, the fair value of borrowings (Level 2) was £931m (2019: £903m).

None of the company's borrowings are secured by charges over assets of the company.

13 Share capital

Allotted, called up and fully paid	**2020** **£m**	2019 £m
5,105,581,781 ordinary shares of £0.0001 each	**1**	1

Each share carries the right to one vote on a poll. The right to vote is determined by reference to the register of members. All dividends shall be declared and paid according to the amounts paid up on the shares. The shares do not carry any rights as respects to capital to participate in a distribution (including on a winding-up) other than those that exist as a matter of law. The shares are not redeemable.

14 Contingent liabilities

Guarantees and letters of credit

Group undertakings have entered into bonds and guarantees in the normal course of business. No liability is expected to arise in respect of bonds, guarantees or letters of credit.

15 Related party transactions

The company is exempt under FRS 101.8(k) from disclosing transactions with Quadgas Holdings TopCo Limited and its subsidiary undertakings where all of the voting rights are held within the group. There were no related party transactions with other companies.

Details of key management compensation are provided in note 7 to the consolidated financial statements.

16 Ultimate parent company

The ultimate parent and controlling company is Quadgas Holdings TopCo Limited and the immediate parent company is Quadgas PledgeCo Limited. The largest and smallest Group which includes the company and for which consolidated financial statements are prepared are headed by Quadgas Holdings TopCo Limited and Quadgas HoldCo Limited respectively. Quadgas Holdings TopCo Limited is registered in Jersey and Quadgas HoldCo Limited is registered in England and Wales.

Copies of Quadgas HoldCo Limited's consolidated financial statements can be obtained from the Company Secretary, Quadgas HoldCo Limited, Ashbrook Court, Prologis Park, Coventry, CV7 8PE.

Copies of Quadgas Holdings TopCo Limited's consolidated financial statements can be obtained from the Company Secretary, Quadgas Holdings TopCo Limited, 3rd Floor 37 Esplanade, St. Helier, Jersey, JE1 1AD.