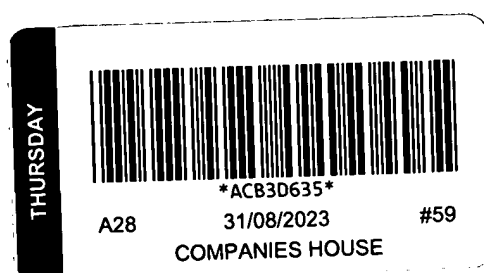


REGISTERED NUMBER: 11050000 (England and Wales)

Group Strategic Report, Directors' Report and
Audited Consolidated Financial Statements for the Year Ended 31 March 2023
for
SGN Midco Limited



SGN Midco Limited (Registered number: 11050000)

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for the Year Ended 31 March 2023

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SGN Midco Limited

Company Information
for the Year Ended 31 March 2023

DIRECTORS:

Charlotte Brunning
Nicholas Robin Salmon (Chair)
Michael Botha
Martin Catchpole
Rebecca Lumlock
Felipe Ortiz
Charles Thomazi (Alternate)
Paul Trimmer
Christian Fingerle
Jeffrey Rosenthal
Michael Oswald Smart
Antoine Kerrenneur

SECRETARIES:

Nicola Shand
Sharmila Sylvester

REGISTERED OFFICE:

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REGISTERED NUMBER:

11050000 (England and Wales)

AUDITOR:

Ernst & Young LLP
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London
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SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

This strategic report sets out the main trends and factors underlying the development and performance of SGN Midco Limited (the "**Company**") and its subsidiaries, outlined below, (together the "**Group**") during the year ended 31 March 2023 as well as those matters which are likely to affect its future development and performance.

THE BUSINESS, ITS OBJECTIVES AND STRATEGY

The Company is a wholly-owned subsidiary of SGN PledgeCo Limited, which in turn is a wholly-owned subsidiary of Scotia Gas Networks Limited ("**SGN**"). Scotia Gas Networks Limited is owned by Apple Newco Limited (37.5%) which is indirectly wholly-owned by Ontario Teachers' Pension Plan Board, UK Gas Distribution 2 Limited (37.5%), which is indirectly owned by Brookfield Super-Core Infrastructure Partners, and Speyside Bidco Limited (25.0%) which is wholly-owned by funds managed by Global Infrastructure Partners (GIP).

References to the "**Trading Entities**" throughout this Report mean Southern Gas Networks plc, Scotland Gas Networks plc and SGN Natural Gas Limited.

The Group comprises SGN MidCo Limited, Southern Gas Networks plc, Scotland Gas Networks plc, SGN Natural Gas Limited and SGN Contracting Limited. Southern Gas Networks plc and Scotland Gas Networks plc are the main trading companies and operate two of the eight regional gas distribution networks in Great Britain. Their gas distribution networks comprise approximately 72,000 kilometres of gas mains delivering natural gas to almost 6 million domestic, commercial and industrial customers. SGN Natural Gas Limited is one of three regional gas distribution networks in Northern Ireland. SGN Contracting Limited is non-trading at present.

Objectives and Strategy

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

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

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

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

Our purpose is to keep everyone safe and warm. As outlined in our RIIO-GD2 business plan, our strategy is to deliver long-term value for existing and future customers, stakeholders and shareholders. This strategy is based on strong financial management and a governance framework, and underpinned by our detailed business plan and five strategic pillars:

1. Delivering safe and efficient service

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

2. Making a positive impact

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

3. Building a shared future

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

4. Creating value and growing our service

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

5. Focusing on talent, skills and opportunities for our people

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

External and regulatory environment

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

The primary legislation controlling the Trading Entities activities as a gas transporter is the Gas Act 1986 (as amended). Under the Gas Act, the Trading Entities hold licences that allows them to operate the gas distribution network they own. Southern Gas Networks plc and Scotland Gas Networks plc are regulated by Ofgem, whereas SGN Natural Gas Limited is regulated by UREG.

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

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Group Strategic Report
for the Year Ended 31 March 2023

Factors affecting the business

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

- **Regulatory price controls**

As outlined above, the prices that can be charged for the use of the Group's networks are determined in accordance with regulator approved price controls these are set by the Trading Entities regulators Ofgem and UREG.

The year ended 31 March 2023 was the second year of the RIIO-GD2 price control, which set the key elements of revenue, outputs and allowed returns until 31 March 2026. Additionally, the regulatory price controls include an allowed rate of return for the investment the Group makes in the network. The allowed rate of return represents the return on debt and equity capital.

- **Safety and reliability of the networks**

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

For all of us at SGN, last August will be remembered for an explosion in Galpin's Road, south London, which tragically claimed the life of a young girl and left several people with injuries. The Company is continuing to support the police and Health and Safety Executive with their investigation of this incident.

- **Efficiency**

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

- **Interest rates**

The costs of financing our operations are affected by changes in interest rates as some of the Group's borrowings are held at floating rates. Exposure to changes in interest rates are hedged by holding both fixed rate and inflation-linked borrowings and by holding derivative financial instruments (interest rate swaps, inflation-linked swaps and cross-currency swaps) where necessary to achieve the desired profile of interest rate risk. The cost of new debt raised by the Group is also affected by changes in interest rates. The Group aims to partially mitigate this risk by maintaining a smooth debt maturity profile to minimise annual refinancing requirements and spread future refinancing risk.

- **Inflation rates**

The value of the Group's regulated assets and its turnover are linked to inflation, which is measured by the Consumer Prices Index including owner occupiers' housing costs ("CPIH"). A large part of the Group's cost base is also linked to various measures of inflation. The costs of financing our operations are also affected by changes in inflation rates as some of the Group's debt has principal and interest payments linked to either RPI or CPI. In addition, the Group is party to a variety of inflation-linked swaps, which have two payment legs linked to CPI. As such, the Group's financial performance, including its performance against various covenants, can fluctuate with inflation.

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

PRINCIPAL RISKS AND UNCERTAINTIES

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

Our current principal risk profile consists of 12 risks reflecting the changing nature of the business environment, political and regulatory environment, RIIO-GD2 strategic objectives and other external risks.

To ensure that the Group focuses on the right risks as we work to build a thriving and enduring business, our principal risks are to be fully reassessed (and our associated risk appetite considered) in the first half of 2023/24 by the Executive Committee and Board.

The principal risks and uncertainties identified are as follows:

Description and Impact of Risk	Mitigation
1. Future of gas network: The shift towards a decarbonised energy system presents several risks to our business model, funding, regulatory framework and organisational capability as decisions from government on climate change expected to lead to an outcome being one that does not rely on natural gas.	<ul style="list-style-type: none">- Active in influencing government and industry stakeholders to lobby for hydrogen rollout.- Creation of the Strategic Hydrogen Executive with other GDNs.- Delivering the SGN evidentiary framework and developing plans for heat decarbonisation rollout.- Utilising innovation funding and working with others to test and deliver evidence for potential decarbonisation pathways.- Developing plans to develop hydrogen storage and production investment opportunities.
2. Cyber and IT resilience: Failure to implement appropriate security risk management and crisis management could result in cyber-attacks from nation states, hacktivists, criminals, and/or insiders.	<ul style="list-style-type: none">- Cyber security investment programme in place and funding requests made for next stage of the programme.
Loss of critical IT services due to the design of core services and/or ineffective Business Continuity Management plans.	<ul style="list-style-type: none">- Increased in-house security team and enhanced managed security service.

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Group Strategic Report
for the Year Ended 31 March 2023

Description and Impact of Risk (cont.)	Mitigation (cont.)
<p>Loss of IT services could result in interruption or disruption to our core business operations.</p>	<ul style="list-style-type: none"> - Compliance with the Network and Information Systems (NIS) Regulation. - Ongoing work to maintain and improve business continuity and disaster recovery procedures. - Hardware and network resilience/segmentation in place. - Maintenance plan and activities in place to manage the risk of IT failure. - Raising staff security awareness through regular training and awareness campaigns. - Participation in audits and exchanges on learnings and best practices.
<p>3. Political and public policy: There is a risk that adverse future intervention by the UK and Scottish Governments in the energy markets, or changes in governmental policy, may have an unfavourable impact on our business model.</p>	<ul style="list-style-type: none"> - Contributing to development of UK and Scottish Government policy. - Continuing to build capability to explain our role and how we contribute to delivery of government policy ambitions. - Targeted engagement with local authorities to develop decarbonisation plans. - Assessment of Scottish independence risk/opportunity to the Group.
<p>4. Leadership, people and culture: Failure to maintain a sufficiently competent, diverse and productive workforce with effective relationships and enough talent. Also, the failure of the leadership team to recognise the changing external and internal environment and indifference to business risks.</p>	<ul style="list-style-type: none"> - Training and development including talent management programmes, which are being reviewed to ensure future fit. - Recruitment of the required number of operational, front-line employees has been made a company-wide priority. - Outsourcing of some training to approved suppliers.

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

Description and Impact of Risk (cont.)	Mitigation (cont.)
	<ul style="list-style-type: none">- Responding to regulatory, supplier and technology developments which may impact on Group strategy.- Three-year pay deal protecting employees against inflationary pressures, plus attract and retain people.- Retraining and recruiting in synchrony with the hydrogen transition.
5. Safety and Health: Failures in the design or implementation of the safety and health management systems may result in unsafe behaviour and working practices.	<ul style="list-style-type: none">- Health and Safety is our number one priority, and we continue to focus on the Group's safety culture.- Continued focus on safety across all assets and operations, including any changes related to a transition to hydrogen.- Track a range of safety metrics very closely and have programmes in place to drive improvements.- Review lessons learnt from major incidents in order to prevent such things from recurring.- Compliance is supported by independent inspections and an audit programme.- Run wellbeing programmes and campaigns for our people.- Emphasis on leading indicators.
6. Financing: The risk that the Company is unable to, or that it costs the Company materially more to raise equity or external debt financing to refinance existing debt or to fund further investment within the group.	<ul style="list-style-type: none">- The Group has a treasury policy which aims to maintain:<ul style="list-style-type: none">• 12 to 18 months' committed sources of liquidity (cash and committed facilities);• A smooth debt maturity profile to minimise annual refinancing requirements and spread refinancing risk;• Access to diversified sources of funding;• A proportion of direct or synthetic inflation-linked debt liabilities.- Regular internal monitoring and reporting of key credit metrics and financial covenants to the Board.

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Group Strategic Report
for the Year Ended 31 March 2023

Description and Impact of Risk (cont.)	Mitigation (cont.)
	<ul style="list-style-type: none"> - Annual results presentations intended for debt investors. - A flexible dividend distribution policy linked to maintaining credit metrics.
<p>7. Environment and climate adaptations: As we move to a zero-carbon economy there is a risk of failing to assess and manage changes as a result of climate change impacts, zero-carbon legislation and policy, market and investor requirements and technological change.</p>	<ul style="list-style-type: none"> - Delivering the Environmental Action Plan and Environmental Sustainability Strategy. - Engaging with the supply chain to support their journey of decarbonisation and environmental improvement. - Regular interaction with stakeholders and customers including collaboration with SGN Environment Advisory Panel. - Engaging with peers and other companies in the energy and infrastructure sectors to enable a best practice approach. - Maintaining our ISO14001:2015 Environmental Management System certification. - Understanding and assessing climate risk to occupied sites and our network. - Pilot projects to demonstrate the safe, efficient and effective transport, storage and use of hydrogen.
<p>8. Legal and compliance: Legal risk is the risk of financial or reputational loss that can result from lack of awareness or misunderstanding of, or ambiguity in, the way law and regulation apply to our business, its relationships, processes, products and services.</p>	<ul style="list-style-type: none"> - Programmes to strengthen our compliance framework, supported by risk-based training programmes. - Code of Conduct and compliance policies covering controls. - Speak Up (Whistleblowing) Policy. - Contracts include compliance clauses.

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Group Strategic Report
for the Year Ended 31 March 2023

Description and Impact of Risk (cont.)	Mitigation (cont.)
	<ul style="list-style-type: none"> - Training and communications to guide and support our people to meet legal and regulatory requirements. - Ongoing assessments to help manage compliance risks associated with business change/developments. - Annual Compliance Report.
<p>9. Supply chain: The risk of disruption to supply continuity if there is over-dependence on a limited number of suppliers and/or failure to meet increased expectations for sustainable procurement due to lack of lack of co-ordination with supplier partners.</p>	<ul style="list-style-type: none"> - Developing and harnessing new suppliers to encourage competition, innovation and resilience. - Supplier performance management and compliance across key areas. - New Logistics team in place to prepare for migration of Logistics service from existing Managed Services Agreement provider. - Ongoing support and management of contracts and supply chains. Planning to deal with short and long-term shocks. - Online sourcing and contract management system. - Issued new Sustainable Procurement Code.
<p>10. Network asset management and physical security: Failures in the design and/or implementation of our asset management policy, management and security systems and procedures, or ineffective crisis management causing reputational damage and shareholder dissatisfaction.</p>	<ul style="list-style-type: none"> - Clear asset investment strategy out to March 2026. - Core business processes help ensure that gas supply to the customer is maintained. - Long-term horizon scanning is in place to capture network asset changes. - Robust annual audit programme and site inspections to ensure compliance with our policies and procedures. - Closely track a range of asset and safety related metrics and have programmes in place to drive improvements. - Test resiliency through several activities such as emergency exercises and risk assessment tools.

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

Description and Impact of Risk (cont.)	Mitigation (cont.)
	<ul style="list-style-type: none"> - A physical security upgrade programme designed to meet government agencies' guidelines. - Learning from incidents within the Group and externally.
<p>11. Customer interests: Failure to maintain high levels of customer service, in particular with our most vulnerable customers, could lead to financial penalties, reputational damage, business stagnation and loss of trust with a range of stakeholders from local communities to national government.</p>	<ul style="list-style-type: none"> - Customer Experience GD2 project, utilising customer insight to ensure we are meeting customer expectations. - Focused training plans to embed processes and upskill our people to deliver the best. - Vulnerable Customer Strategy to harness new partners and encourage innovation for services and communications. - Ongoing support and management of external relationships to maximise collaboration and co-operation. - Contributing, together with all stakeholders, to the development of a fair and affordable transition.
<p>12. Licence conditions: Failure to comply with our licence conditions and obligations.</p>	<ul style="list-style-type: none"> - Governance and compliance frameworks to deal with issues and developments arising from price controls. - Experienced regulation, finance and legal teams. - Engaging with all levels of Ofgem and government. - Delivery of regulatory outputs is measured and monitored on a regular basis. Action plan put in place to ensure Emergency Response KPIs that were missed in financial year 22/23 are achieved in the coming year. - Annual Compliance Report. - Improved data analytics and predictive models including to inform resourcing requirements.

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Group Strategic Report
for the Year Ended 31 March 2023

Business Unit Leadership are responsible for identifying, responding to, monitoring and assuring key risks. Business Units are supported by the Risk function.

Our Risk and Resilience Committee includes representation from all parts of the business with a mixture of the Executive team and Senior Leadership. The Risk and Resilience Committee supports the Executive team by overseeing the operational risk registers and making recommendations. It meets quarterly to review SGN's current and future risk profile and resilience capabilities.

The Executive owns and oversees the enterprise risk management framework. Each principal risk is assigned an Executive risk owner who is responsible for monitoring the exposure and nature of the risk, deciding how it should be managed and taking the necessary action to bring it back to the desired target level. The Executive receives formal updates following the Risk and Resilience Committee and are supported by the Risk function to ensure ongoing risk management.

The Board has overall responsibility for making sure that we manage risk within acceptable limits. Our most significant risks are reported to the Board on a bi-monthly basis by our CEO and semi-annually the Board carries out a review of the full principal risk register. The Board is supported by the Audit Committee, who oversees internal controls within the Group. The Board also considers new or emerging risks and recommends ways to tackle them.

Enhancing our risk framework

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

SGN Midco Limited (Registered number: 11050000)**Group Strategic Report**
for the Year Ended 31 March 2023**TCFD REPORT**

Climate change presents financial risk to the global economy. Financial markets require clear, comprehensive, high-quality information on the impacts of climate change. This includes the risks and opportunities presented by extreme weather events, rising temperatures, climate-related policy, and emerging technologies in our changing world.

The Financial Stability Board (FSB) created the Task Force on Climate related Financial Disclosures (TCFD) to improve and increase reporting of climate-related financial information. As per Companies Act (2006), for companies with >500 employees and >£500m turnover, it is mandatory to report in alignment with TCFD for periods beginning on or after 6 April 2022.

The Group has focused its efforts over the last financial year to provide disclosures aligned with the TCFD framework. We are therefore pleased to present our responses to each of the recommended disclosures below. We appreciate that this reporting is part of our sustainability journey, and during this first phase of TCFD reporting, we have identified areas for further development. For additional detailed information on risks, please refer to 3rd Round Climate Change Adaptation Report, which can be accessed from the SGN website at

https://www.sgn.co.uk/sites/default/files/media-entities/documents/2022-01/SGN-ARP3-1221_0.pdf.

Disclosure recommendation	Alignment with TCFD	Section reference	Page
Governance			
Describe the Board's oversight of climate-related risks and opportunities	Partial	Principal risks and uncertainties; TCFD	5-10 12-18
Describe management's role in assessing and managing climate-related risks and opportunities	Partial	Principal risks and uncertainties; TCFD	5-10 12-18
Strategy			
Describe the climate-related risks and opportunities the organisation has identified over the short, medium and long term	Partial	TCFD	12-18
Describe the impact of climate risks and opportunities on the organisation's businesses strategy and planning	Partial	TCFD	12-18

SGN Midco Limited (Registered number: 11050000)Group Strategic Report
for the Year Ended 31 March 2023

Disclosure recommendation (cont.)	Alignment with TCFD (cont.)	Section reference (cont.)	Page
Describe the resilience of the organisation's strategy taking into consideration different climate-related scenarios, including a 2°C or lower scenario	Not included at this stage	TCFD	12-18
Risk management			
Describe the organisation's processes for identifying and assessing climate-related risks	Partial	Principal risks and uncertainties; TCFD	5-10 12-18
Describe the organisation's processes for managing climate-related risks	Partial	TCFD	12-18
Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management	Partial	Principal risks and uncertainties; TCFD	5-10 12-18
Metrics and targets			
Disclose the metrics used by the organisation to assess climate-related risk and opportunities in line with its strategy and risk management process	Fully	Environment and sustainability; TCFD	36-37 12-18
Disclose Scope 1, Scope 2 and, if appropriate, Scope 3 greenhouse gas emissions and the related risks	Fully	Environment and sustainability; TCFD	36-37 12-18
Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets	Fully	TCFD; Annual Environmental Report on SGN website; ESG Report of the Group's ultimate parent undertaking, Scotia Gas Networks Limited	12-18

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Group Strategic Report
for the Year Ended 31 March 2023

Governance

Board oversight

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

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

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

Management's role

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

Overall management level responsibility for sustainability, including the strategic risk of climate change, sits with the Director of Stakeholder Relations and Communication and the Head of Sustainability. Risks are assessed through a comprehensive risk management system and each directorate has its own risk register. Climate-related risk and opportunity management is devolved to the different directorates through the risk registers, where 'environment' is one of the impact measures.

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

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

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

Strategy

Climate risks and opportunities over time

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

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

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

- Weather events that have an impact on the integrity of the network or damage to assets, such as flooding (coastal, fluvial, pluvial and/or groundwater).

Whilst many of our assets will function under water for a period of time, the ability to maintain them is critical. Waterlogged ground can have a detrimental effect on the degradation of assets. For example, a pipeline project in Dunkeld, in our Scottish network, was born out of the need to re-route a below-ground pipeline that had been exposed by fluvial flooding due to its close proximity to a river. Physical risks to our assets have been more closely examined and reported on in our 3rd Round Climate Change Adaptation Report.

- Above ground assets, for example governors, are also important to include when preparing physical risk assessments.
- Prolonged heat and cold weather events can impair equipment and impact supply chain, for example ability to access sites.
- Chronic longer-term changes to weather patterns could impact natural gas demand and management of peak demand versus underutilisation of the network.
- Extreme weather events may impact on the health, safety and wellbeing of colleagues, particularly those who are field based.

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

Policy and regulation

This is expected to increase over time. Currently the following key risks have been identified:

- net zero targets for the UK and Scottish governments as per relevant Climate Change Acts;
- ban on new petrol and diesel vehicles by 2030;
- potential carbon taxes;
- emerging regulation on increased sustainability reporting and disclosure.

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Group Strategic Report
for the Year Ended 31 March 2023

Market

Natural gas demand may be impacted by market pressures.

Another risk would be around people skills and experience: we will need to ensure we have the right skilled resource to work with emerging decarbonised technology. This in turn adds to competition in the market for the right people with the right skills.

Government strategic decision on hydrogen in 2026, on how significant a role hydrogen will have in decarbonising domestic heat.

Reputation

As a gas distribution network, we acknowledge that there are reputational risks in being associated with the fossil fuel industry both in terms of our standing with customers and other stakeholders, such as debt investors and credit rating agencies.

However, this is also an opportunity, as SGN can take a leading role in the decarbonisation of the network.

Technology

Risks identified include:

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

Opportunities identified include:

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

Impact on businesses strategy and planning

Identified risks and opportunities are raised with the Board and can impact business planning. We assess capability, financial, environmental, safety, reputation, and regulatory impacts and these are defined in our risk register.

Significant financial impact is defined as:

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

SGN Midco Limited (Registered number: 11050000)

Group Strategic Report
for the Year Ended 31 March 2023

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

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

Scenario planning

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

Risk management

Processes for identifying and assessing climate-related risks

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

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

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

Managing climate-related risks

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

Integration into overall risk management

The oversight of the enterprise risk management system is Board-led with ongoing input from the Executive leadership team giving visibility to the nature of risks and extent of risks facing the organisation. Oversight of the principal risks (including environment and climate adaptation) remains effective through several established routes during the year.

Each principal risk is assigned an Executive owner who is responsible for monitoring the exposure and nature of the risk, deciding how it should be managed and taking the necessary action to bring it back to the desired target level.

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

Metrics and targets

Metrics

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

In the Directors' Report (page 36-37) we disclose KPIs on our carbon footprint Scope 1, including shrinkage, and Scope 2.

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

Greenhouse gas emissions

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

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

Targets and performance

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

Progress against our greenhouse gas emissions targets and how we are increasing the availability of biomethane in the networks, are set out in the ESG Report of the Group's ultimate parent undertaking, Scotia Gas Networks Limited, which can be obtained from St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ, United Kingdom.

In addition, we have other climate-related targets supporting our environmental strategy, such as developing biodiversity projects to create more healthy green spaces at our sites and depots while also benefitting local communities, aiming to achieve biodiversity net gain. We also engage with and support our suppliers to implement ESG targets and improve their environmental impacts.

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

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Stakeholders

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

Resources

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

The Group's distribution network comprises approximately 72,000 kilometres of gas mains, together with associated services, plant and machinery and storage facilities.

The Group had 4,012 full time equivalent employees at 31 March 2023 (2022: 3,638). It places considerable value on the involvement of employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Group during the year. It continues to invest in the development and training of its people in order to ensure both individual developmental needs and business skill requirements are met.

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SECTION 172(1) STATEMENT

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

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

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

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

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

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

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

Further details on how the SGN Board operates and how it reaches decisions, including some of the matters discussed and debated during the year, are detailed in this section and on pages 38 to 46.

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

Section 172 factors

Directors' consideration of Section 172 Factors

Long-term impact

The UK Government plans for decarbonisation of heat in order to achieve net zero by 2050, and 2045 in Scotland. This presents both an opportunity for the Group to be influential in shaping the future of energy and a challenge. The Group must be able to articulate and execute a robust strategy based on a comprehensive analysis and evaluation of the strategic options in context of likely future states. Establishing a strategic approach and continuing to invest in the future of energy/decarbonisation pathway to achieve net zero will help transition the business to provide a clean energy experience which is key to the Group's vision.

Impact on employees

The Group is committed to providing job security for our colleagues during the energy transition and beyond. In order to do so, the Group continues to work toward proving the viability of future of energy associated projects. To further ensure the success of the strategic approach and keeping our people in mind, the Group provides regular updates on the progress of projects and developments to ensure our people are kept informed and actively encouraged to provide any feedback. More information on how we engage with our people can be found on page 24.

Nurturing business relationships

SGN continues to collaborate and work alongside industry peers, the government, local authorities and Ofgem to support and participate in the development of the UK's pathway to decarbonisation which includes developing pioneering clean energy projects to help shape the UK's future.

Impact on community and environment

The UK's biggest net zero challenge is decarbonising our homes and buildings. It's the second biggest emitting sector with around 30% of our national emissions coming from around 25 million homes which are connected to gas networks across the UK. The decarbonisation of homes will impact our communities, customers and environment. Customer research helps SGN to understand what matters most to our end-users. Our policy and political work linked to our strategy will amplify our hydrogen demonstration projects and establish as the clear and cost-effective pathway to decarbonise heat at lower cost and disruption to end-users, at pace and scale.

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Section 172 factors (cont.)

Enhanced corporate reputation

Acting fairly between members

Directors' consideration of Section 172 Factors (cont.)

SGN continues to create the political space to ensure hydrogen is an option in the UK's energy transition and alongside this, that the Group's reputation is strengthened as a world-leading network in the transition from natural gas to hydrogen.

SGN has three supportive shareholders with each having nominated representation on the Board. The Board seeks to always act fairly between shareholders and treat them equally, including ensuring that adequate procedures are in place to address any conflicts of interests that could arise and ensuring equal access to information. With this in consideration, the Board acknowledges the support from its members and also support the ongoing development of the future of energy strategy to support our customers, the community and the Government's plans in reaching net zero and longevity of the business.

Board decision: Approval of continuing investment in our Cyber Security Programme

Section 172 factors

Long-term impact

Impact on employees

Nurturing business relationships

Directors' consideration of Section 172 Factors

The UK National Cyber Security Strategy 2016-21 identified that cyber-attacks are growing more frequent, sophisticated and damaging. The Group, along with UK Government and Ofgem, recognises the scale of the cyber threat to critical national infrastructure, such as our gas networks.

By not investing in our cyber resilience, we would put our Company at risk of attacks from national states, hacktivists, criminals and/or insiders. Investment is required to ensure our continued cyber resilience against ever-growing threats.

To maximise the effectiveness of our cyber security programme, we continue to raise employee awareness of cyber risks, and how to protect employees and our Company against cyber threats through training and awareness campaigns.

The Group continues to work with industry peers and government agencies to ensure our cyber security programme is robust and complies with relevant directives. The Group also receives learnings and best practice from its shareholders' portfolio companies. Following Russia's attack on Ukraine, the National Cyber Security Centre called on UK organisations (including SGN) to bolster their online defences. Ofgem has also provided a Cyber resilience briefing to the Company and its Board of Directors. The continued investment allows SGN to deliver on stakeholder expectations.

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Section 172 factors (cont.)

Impact on community and environment

Enhanced corporate reputation

Acting fairly between members

Directors' consideration of Section 172 Factors (cont.)

An extreme cyber event could prevent us from distributing gas to our 6 million customers. Investment is essential to ensure our cyber defence continues to adapt and improve to the ever-evolving cyber threat landscape, as well as to minimise the risk and impact of cyber events on our core business.

We must invest in our cyber resilience through the cyber security programme to give us the best chance of mitigating the threat of attacks. An attack on our systems that impacts our ability to keep our customers safe and warm could have a catastrophic impact on our corporate reputation.

SGN's shareholders and the Executive management team fully support the decision to continue investing in cyber security.

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

Section 172 factors

Long-term impact

Impact on employees

Nurturing business relationships

Impact on community and environment

Enhanced corporate reputation

Acting fairly between members

Directors' consideration of Section 172 Factors

In determining whether to accept the GD23 Final Determination, the Directors considered the long-term impact the final determination and supporting licence modifications would have on SGN Natural Gas Limited. Taking into account the full determination, including allowances and all modifications, Directors considered it would be in the long-term interest to accept the overall package.

Directors considered the impact any appeal would have on employees and wider business relationships when considering whether or not to appeal or accept the final determination.

Directors considered whether the final determination was in the best interest of each of its stakeholder group and the wider community. In doing so, Directors considered the impact any appeal would have on the deliverability of the licence requirements.

All shareholders were consulted and supported the decision to accept the GD23 final determination.

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ENGAGING WITH STAKEHOLDERS

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

We encourage genuine two-way engagement with our key stakeholder groups. Stakeholder engagement takes place at both the operational day-to-day level within the business and at Board level, as part of an extensive engagement programme with our six key stakeholders:

- Customers
- Our People
- UK and Scottish governments and Regulators
- Communities and Environment
- Suppliers, Contractors and Partners
- Shareholder and Debt Investors

The Board takes insight from each level of engagement into account in its decision-making process. Following the lifting of Covid-19 restrictions, we conducted a mixture of face-to-face and virtual engagement to ensure that this remained inclusive and allowed for a two-way dialogue with our stakeholders.

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

OUR PEOPLE

We employ approximately 3,800 highly skilled and dedicated people across Scotland, the south of England and in Northern Ireland.

Why we engage

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

How we engage

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

Stakeholder issues raised

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

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Outcomes of engagement on key decisions

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

Key Board decisions

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

CUSTOMERS

We keep gas flowing safely and reliably to 6 million homes and businesses, all day, every day.

Why we engage

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

How we engage

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

Stakeholder issues raised

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

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Outcomes of engagement on key decisions

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

Key Board decisions

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

COMMUNITIES AND THE ENVIRONMENT

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

Why we engage

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

How we engage

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

Stakeholder issues raised

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

Outcomes of engagement on key decisions

- Focused discussion on shrinkage performance, and innovative activities to drive down emissions
- Continued performance reporting on SGN's operations and Repex delivery programme at Board meetings
- Conducted a dedicated Energy Futures strategy session covering hydrogen and the journey to net zero
- Development of the Environmental Action Plan and Communities investment strategy

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Key Board decisions

- Approval to publish our inaugural TCFD report
- Investment in third-party partnerships with strong board support
- Approved further investment into SGN's hydrogen (H100) project
- Agreement to SGN's community support plan for winter 2022

SUPPLIERS, CONTRACTORS AND PARTNERS

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

Why we engage

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

How we engage

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

Stakeholder issues raised

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

Outcomes of engagement on key decisions

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

Key Board decisions

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

GOVERNMENT AND REGULATORS

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

Why we engage

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

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How we engage

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

Stakeholder issues raised

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

Outcomes of engagement on key decisions

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

Key Board decisions

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

SHAREHOLDERS AND DEBT INVESTORS

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

Why we engage

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

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How we engage

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

Stakeholder issues raised

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

Outcomes of engagement on key decisions

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

Key Board decisions

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

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FINANCIAL REVIEW

The Group sets out below its financial review using key performance indicators for the year ended 31 March 2023.

The SGN Midco Group has faced a number of challenges in the second year of the RIIO-GD2 regulatory period, which has impacted financial performance for 2022/23. The biggest challenge was resourcing, particularly in the south of England, caused by an increase in churn following the Covid-19 pandemic and adverse market factors, such as labour shortage, making it a constant challenge to recruit and retain talent. The resourcing challenge has made it difficult to meet our emergency response standards during periods of high call volumes and has required a diversion of engineers away from replacement and connections jobs to support these efforts. However, despite this, the Group failed to meet the 97% target imposed by the Gas Transporter Standard Special Conditions D10 in relation to the time taken to respond to controlled and uncontrolled gas escapes. Consequently, this has resulted in an Operational target provision being recognised in the year ended 31 March 2023 of £13m (2022: £nil).

Turnover for the year ended 31 March 2023 was £1,244m (2022: £1,060m). The majority of turnover was earned from charges made for the provision of gas transportation capacity as well as revenue based upon gas volumes transported in the year. The current year increase is predominantly driven by an increase in our regulated revenue in line with the profile set out within our price control.

Operating profit for the year was £451m (2022: £341m). This year on year increase is largely driven by the increase in turnover noted previously, and partially offset by increased operational costs linked to resourcing difficulties and additional costs incurred in supporting the emergency response efforts.

Profit for the year before taxation amounted to £193m (2022: £80m) and profit for the year after taxation amounted to £143m (2022: £180m loss). The current year tax charge is significantly lower than the tax charge in the prior year. This is mainly due to a change in the main rate of corporation tax from 19% to 25% which has been substantively enacted at the balance sheet date in the prior year and as such deferred tax has been calculated at the higher rate accordingly in financial year 2021/22.

Scotland Gas Networks plc had a £279m RPI-linked public bond that matured in October 2022. The maturity was part-refinanced by a £100m CPI-linked loan put in place in March 2022, which was drawn in September 2022, with the remainder refinanced by £184m of fixed rate private placement notes issued in October 2022. £154m of this issuance was drawn in October 2022 with £30m drawn in March 2023.

Other than repaying a £30m drawing on its RCF in April 2022, Southern Gas Networks plc had no debt maturities during the financial year. In the coming financial year however, Southern Gas Networks plc has a £300m fixed rate public bond maturing in October 2023. To part-refinance this, \$132m (£116m equivalent) of fixed rate private placement notes were issued in October 2022, which were fully drawn in March 2023.

Southern Gas Networks plc put in place additional short-term committed liquidity in June 2023, and further long-term financing will be sought ahead of the October 2023 maturity. Scotland Gas Networks plc and SGN MidCo Limited have no scheduled debt maturities in the coming year.

During the year the Group paid dividends totalling £70m (2022: £104m).

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Capital expenditure (excluding replacement expenditure) during the year amounted to £152m (2022: £118m). The increase resulted from the phasing of spend over the RII0-GD2 period. Capital expenditure is incurred to ensure that the networks continue to operate at minimum agreed pressures and that sufficient storage capacity is available to meet instances of peak demand, as well as when new connections or increased capacity are added to the networks.

Treasury policies and capital structure

The Group's operations are financed by a combination of equity and retained profits, bank loans, private placements and public bonds. The Group's funding and liquidity are managed within a framework of policies and guidelines authorised by the Board of Directors. Further details are set out in the Directors' Report.

As a matter of policy, a minimum of 75% of debt is maintained at either fixed or inflation-linked rates of interest. This policy is kept under review. Derivative financial instruments, including interest rate swaps, inflation-linked swaps and cross-currency swaps are used, where necessary, in order to achieve this desired profile.

Pension commitments

A large proportion of the Group's employees are members of the Scotia Gas Networks Pension Scheme which provides final salary defined benefits for members. The Group accounts for any pension asset or liability in accordance with FRS 102. The net pension surplus as at 31 March 2023 was £246m (2022: £362m). The Group's normal pension contributions remain at 37.3% in line with previous years. Until 31 March 2022 additional contributions were paid annually to repair the actuarial deficit in the defined benefit pension scheme, however from 1 April 2022 these deficit contributions are no longer payable (2022: £12.5m).

Liquidity risk

Liquidity is maintained through a mixture of long-term borrowings and short-term liquid funds in order that there are sufficient funds available for the Group's current and planned operations. Committed facilities are in place in order to provide funding for future capital and replacement expenditure as well as to provide sufficient available facilities to meet the seasonal working capital requirements of the Group. The revolving credit facility totalled £360m for the Group (2022: £360m) and is in place until March 2025; as at 31 March 2023 £360m was undrawn (2022: £330m). The debt service reserve liquidity facility held at SGN MidCo Ltd remained undrawn throughout the year and was extended for a further 364 days to 10 January 2024.

Counterparty credit risk

The Group transacts with banks for the provision of deposits, interest rate, inflation and currency hedging transactions. Under the Group's hedging policy, counterparties must maintain minimum credit ratings with appropriate collateral posting and replacement thresholds based on each counterparty's long-term credit ratings. At the year end the Group had £116m (2022: £131m) payable relating to financial instruments with bank counterparties.

In respect of short-term cash management, counterparties are subject to review and approval according to defined criteria, with limits set on both the aggregate amount of investment and the investment term based on the credit rating of the counterparty. All investment counterparties must carry a minimum long-term credit rating of A- or equivalent for the Group to enter into a new transaction.

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Dividend policy

The Group's policy is to manage the level of distributions after taking into consideration the expected cash flows and investment plans across the business, the level of committed funding available as well as the financial covenants and credit metrics of the Group and targets set by the Board. The inherent risk in the business and the wider economy is also considered.

Accounting policies

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

OPERATIONAL REVIEW

Safety

Injury performance

The Group's overriding goal is to distribute gas safely and reliably and to ensure a safe workplace for its workforce with everyone striving towards eliminating injuries. This year the lost time injury performance rate was 0.07 injuries per 100,000 hours for the year ended 31 March 2023 (2022: 0.06).

Board responsibility

The Board has a Safety, Health and Environmental Advisory Committee that is responsible for monitoring health and safety performance and ensuring the health and safety policy statement is adhered to. The Committee provides the Board with reports on any key areas identified.

Gas mains replacement programme

The Group replaces the iron pipes with modern polyethylene pipes to improve the safety of the existing network. Replacement expenditure, primarily of iron pipes, was £257m in the year to 31 March 2023 (2022: £229m). The increase in value was due to a rise in contractor rates. This financial year, due to resourcing constraints, our replacement works focused mainly on the key risk areas. We have worked hard to complete these jobs in a timely manner to minimise the impact on our customers.

Gas escapes standards of service

The Group's engineers respond to reports of suspected gas leaks 24 hours a day, 365 days a year, regardless of from whom people buy their gas. Its engineers aim to attend all uncontrolled gas escapes within one hour and all controlled gas escapes within two hours. Uncontrolled gas escapes are defined as those where the smell of gas persists and where the gas supply is still 'on' at the time the customer calls. We responded to over 126,400 uncontrolled and 58,400 controlled gas escapes during the year ending 31 March 2023.

Due to an intense cold snap pre-Christmas resulting in unprecedented surge in calls, along with other contributing factors and despite our best efforts, the Group's engineers failed to meet the 97% target imposed by the Gas Transporter Standard Special Conditions D10 in relation to the time taken to respond to controlled and uncontrolled gas escapes. This has been the first time in the Group's history to miss these targets. During the year ended 31 March 2023 we attended 94.5% (2022: 98.0%) of uncontrolled gas escapes within one hour and 94.5% (2022: 99.2%) controlled gas escapes within two hours. Based on historical cases from other Gas Distribution Networks, this is expected to result in a fine and as such an Operational target provision has been recognised in the year, as outlined on page 30.

We have an action plan in place to ensure that Emergency Response KPIs are achieved in the coming year.

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Gas networks' regulation

The year ended 31 March 2023 was the second year of the RIIO-GD2 price control, which set the key elements of revenue, outputs and allowed returns until 31 March 2026.

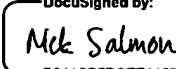
Revenues are earned through charges levied on network users, to cover costs and earn a return on the network company's regulated assets. Ofgem also has incentives in the price control to encourage greater efficiency, innovation and delivery of an enhanced standard of service for customers.

Gas network companies in Northern Ireland are subject to similar regulation and price controls which are set by their Regulator UREG. The GD17 price control period ended on 31 December 2022 and was succeeded by the GD23 price control which is applicable from 1 January 2023 until 31 December 2028.

Further details

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

APPROVED BY THE BOARD AND SIGNED ON ITS BEHALF BY:

DocuSigned by:

B0440B5B0EE1459:.....
Nicholas Robin Salmon (Chair) - Director

Date: 27-07-23 | 11:54 AM BST
.....

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

PRINCIPAL ACTIVITY

The Group's principal activity is the development, administration, maintenance and operation of the Scotland, Northern Ireland and South and South East of England gas distribution systems and the supply of transportation services in these areas. It will continue in this activity for the foreseeable future.

DIVIDENDS

The Group paid an interim dividend of £70m (2022: £104m). The Directors do not recommend the payment of any final dividend for the year (2022: £nil).

FUTURE DEVELOPMENTS

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

EVENTS SINCE THE END OF THE YEAR

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

DIRECTORS

The directors shown below have held office during the whole of the period from 1 April 2022 to the date of this report.

Charlotte Brunning
Nicholas Robin Salmon (Chair)
Michael Botha
Martin Catchpole
Rebecca Lumlock
Felipe Ortiz
Charles Thomazi (Alternate)
Paul Trimmer

Other changes in directors holding office are as follows:

Christian Fingerle - appointed 27 May 2022
Jeffrey Rosenthal - appointed 14 June 2022
Michael Oswald Smart - appointed 27 May 2022
Antoine Kerrenneur - appointed 29 March 2023

REVIEW OF BUSINESS

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

DIRECTORS' INSURANCE AND INDEMNITIES

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

FINANCIAL RISK MANAGEMENT

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

Interest rate risk

The Group has interest bearing liabilities, and as a matter of policy a minimum of 75% of debt is maintained at either fixed rate of interest or inflation linked. The Group uses interest rate swaps, where necessary, in order to achieve this desired profile. The Company uses derivative financial instruments, including interest rate swaps, inflation-linked swaps and cross-currency swaps, where necessary, in order to achieve this desired profile.

Inflation rate risk

The Group's regulated asset base and turnover are linked to inflation as measured by CPIH, which can decrease as well as increase. The Group partially manages this risk by maintaining a level of inflation-linked debt, whereby the interest and final principal payment on this debt is linked to inflation. As a matter of policy, the Group aims to maintain around 35% of its debt portfolio in inflation linked. The Group also uses inflation-linked swaps, where necessary, to achieve this profile. This policy is kept under review and is updated as deemed necessary by the Board.

Foreign exchange risk

The majority of the Group's borrowings are denominated in Pound Sterling, so there is no foreign exchange risk on these borrowings. In accordance with its covenants and Group policy, when the Group raises finance in currency other than Pound Sterling, cross currency swaps are used to fully hedge all non-Sterling denominated borrowings into Pound Sterling.

\$132m (£116m equivalent when swapped) of fixed rate private placement notes were issued in October 2022, which were fully drawn in March 2023. In October 2022, the Group entered into \$132m (£116m equivalent) of cross-currency swaps to fully convert the US dollar principal and interest payments into Pound Sterling on the above-mentioned debt issuance.

The Group is party to contracts for the provision of various goods and services where the payment currency for the contract is not in Pound Sterling. The Group may enter into short-term foreign exchange transactions, including derivative financial instruments, to hedge any foreign exchange risk arising from payments under these contracts.

Liquidity risk

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

Credit risk

The Group transacts with banks for the provision of interest rate and inflation rate hedging transactions. The Group takes reasonable steps to maintain a minimum credit rating requirement as set out in its hedging policy. In respect of short-term cash management, counterparties are subject to review and approval according to defined criteria. Trade receivables predominantly relate to transportation income from gas shippers. Credit risk arising from the Group's regulated business is managed in accordance with industry standards as set out by the Unified Network Code. Credit risk on amounts receivable from other Group companies is considered minimal.

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Pricing risk

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

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

EMPLOYEES

The Group places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the Group. Participation by employees generally is encouraged through team meetings, briefings, an internal newspaper and an intranet site. Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests.

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

GOING CONCERN

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

The directors have forecast cash flows of the Group for the next twelve months to 31 July 2024 (the going concern period) and have obtained a support letter from Scotia Gas Networks Limited confirming that it can and will support the Company in meeting its liabilities throughout the going concern period.

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

Consequently, the Directors believe that the Group will be able to meet its liabilities as they fall due and will have adequate resources to continue in operational existence for twelve months (to 31 July 2024) from the date of approval of this report. Accordingly, the Directors continue to adopt the going concern basis in preparing the financial statements.

ENVIRONMENT AND SUSTAINABILITY

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

SGN Midco Limited (Registered number: 11050000)Directors' Report
for the Year Ended 31 March 2023

	2022/23		2021/22		Annual Movement Decrease/ (increase)	
	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover	Tonnes of CO ₂ e	Tonnes of CO ₂ e per £1m turnover
Scope 1						
Energy consumption (excluding electricity)	3,144	2.53	5,106	4.82	1,962	2.29
Transport (direct commercial vehicles and business miles)	13,667	10.99	17,140	16.17	3,473	5.18
Scope 2						
Electricity consumption	32	0.03	128	0.12	96	0.09
Scope 3						
Rail, air and ferry travel	31,860	25.61	19,303	18.21	-12,557	-7.40
Total (excl. shrinkage)	48,703	39.16	41,677	39.32	(7,026)	0.16
Shrinkage	96,635	560.00	721,447	680.61	24,812	120.61
Total carbon emissions	45,338	599.16	763,124	719.93	17,786	120.77

Data has not been independently verified. Data provided here is in line with annual regulatory reporting of carbon footprint to Ofgem using Defra conversion factors. It includes data from our Southern and Scotland networks. Conversion factors are updated annually. Where market-based factors are stated these are provided annually by our electricity suppliers. Total annual net emissions figure uses market-based methodology.

Natural gas shrinkage is made up of leakage of natural gas (which contains the greenhouse gas methane) from the network, own use of gas and theft of gas. This is the biggest part of the Group's carbon footprint accounting for 93.5% (2022: 95.0%). Reducing shrinkage therefore has the largest effect on reducing our carbon footprint. Over the year the Group have achieved a 3.4% reduction in natural gas shrinkage (2022: 2.3%) which equates to 24,812 tonnes of CO₂ equivalent (2022: 12,353). The reductions are largely achieved through our iron mains replacement programme, optimising and driving down operating pressures in the network, gas conditioning and investment and innovation.

Scope 1 gas usage from occupied/operational sites is low compared to FY22. This is due to our biggest contributor to gas consumption, a Turbo Expander and associated combined heat and power boiler, having been off due to maintenance in the Summer of 2022. At 31 March 2023, the equipment was operational again, but after the balance sheet date, in April 2023, it was switched off for improvement works. At the date of this report it is not yet known when these works will be completed. The levels of emissions for Scope 1 Energy consumption are expected to return to former levels once the equipment is operational again.

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

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

STATEMENT OF CORPORATE GOVERNANCE ARRANGEMENTS

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

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

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

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

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

Accordingly, the Directors have regard to what controls, in their judgement, are appropriate to the business, to the materiality of the risks inherent in the business and to relative costs and benefits of implementing specific controls. Internal control is maintained through an organisation structure with clearly defined responsibilities, authority levels and lines of reporting, the appointment of suitably qualified staff in specialised business areas and continuing investment in high-quality information systems. These methods of control are subject to periodic review as to their implementation and continued suitability. There were no changes in the Group's internal controls over financial reporting during the year covered by this report that has materially affected, or is reasonably likely to materially affect, the Group's internal control over financial reporting.

Internal audit

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

Wates Principles

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

The governance framework will also provide the right environment for the Board to make decisions for the long-term success of the Group. Throughout FY 2023/24, the Board will continue to review and challenge how the Group can continue to improve its corporate governance.

The six Wates Principles are as follows:

1. Purpose and leadership

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

2. Board composition

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

3. Director responsibilities

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

4. Opportunity and risk

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

5. Remuneration

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

6. Stakeholder relationships and engagement

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

Corporate Governance

In the following section of the Directors' Report, we describe how we have applied the Wates Principles in line with its 'comply or explain' model and confirm full compliance with its principles for the reporting year ended 31 March 2023:

Principle 1 - Purpose and leadership

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

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

During the financial year, the Group's employees, the Executive Committee and the Board were engaged to establish the refreshed purpose, vision and values as represented above. More than 1,300 colleagues were involved in this engagement programme. Looking ahead we will be developing our strategy out to 2030 to underpin our purpose, vision and stand as an organisation.

Principle 2 - Board composition

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

The Board comprises eight Non-Executive Directors, including a separate Chair to the Chief Executive, to ensure that the balance of responsibilities, accountabilities and decision making across the Group are effectively maintained. The Chief Executive, Chief Financial Officer and Company Secretary attend each Board meeting. Two Independent Non-Executive Directors also sit on the subsidiary Boards of Scotland and Southern Gas Networks plc.

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

At the start of the financial year, the Group's newly appointed six Directors undertook a comprehensive induction programme. These Directors bring a wealth of experience and come from a range of backgrounds. The Board continues to remain committed to improving diversity throughout the Company in terms of gender, ethnicity, disability and age. This matter falls within the remit of the Board however its newly formed Board sub-committee, the Nomination Committee, actively engages with the shareholders to ensure that diversity remains a key objective for the selection and appointment of Directors.

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

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

Principle 3 - Director responsibilities

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

The Board continues to be supported by the work of the Board Committees. The Board Reserved Matters continues to be rolled out, to ensure the balance of responsibilities, accountabilities and decision making is maintained between the Executive Committee and the Board.

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

Principle 4 - Opportunity and risk

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

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

The Board formally reviewed and challenged key principal risks and received bi-monthly updates on those with a high residual risk rating. The Board also reviewed key investment opportunities. Our key principal risks are to be fully reassessed and associated risk appetite considered in the first half of 2023/24 with the Board.

Principle 5 - Remuneration

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

The newly formed Remuneration Committee (previously the People & Reward Committee) has clearly defined terms of reference and is responsible for making recommendations to the Board concerning the Group's remuneration strategy, recruitment framework and long-term incentive plans for senior Executives. The Committee takes advice from independent external consultants who provide updates on legislative requirements, best market practice and remuneration benchmarking. The primary objective is to set remuneration at a level that will enhance the Group's resources by securing and retaining quality people who can deliver our purpose, vision and values and long-term goals for its existing and future stakeholders.

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

Principle 6 - Stakeholder relationships and engagement

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

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

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

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

Chair

Our Board is led by our Chair, Nick Salmon, who was appointed on 1 March 2021 and is responsible for the effective running and management of the Board. The roles of Chair and Chief Executive Officer are separate, with clear divisions of responsibilities.

Board of Directors

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

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

Board constitution and appointments

The Board of Directors comprises eight Non-Executive Directors. This consists of a Non-Executive Chair and seven Non-Executive Directors. The Board of Directors is the same for the Company and each subsidiary company within the Group, except for Scotland Gas Networks plc and Southern Gas Networks plc, which consist of two additional independent Non-Executive Directors.

Each of the non-executive Directors are chosen for their diversity of skills and experience.

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

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

Roles and responsibilities for each Board Member, Chief Executive Officer, Chief Financial Officer and Group Company Secretary can be found on page 57 followed by their biographies on page 58-60.

Board Committees

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

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

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

Further information on the Board committees is set on pages 47 to 54.

Board effectiveness

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

Chief Executive Officer and Chief Financial Officer

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

Executive Committee

In FY 2022/23 the decision was made to split the Executive Committee into two forums, the Operational Executive Committee, and the Strategic Executive Committee. This was to ensure that the appropriate level of focus was given to Operational Performance and Strategic Planning respectively. The day-to-day management of the Company is delegated to these Committees, which meet monthly and is chaired by the Chief Executive Officer and whose membership includes the Chief Financial Officer and leaders of each business unit. Both Committees are in turn supported by their own operational and assurance framework, with defined roles and responsibilities including relevant delegated authorities.

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Board and Executive Reporting

To ensure that all decision making is well-informed, transparent and balanced, careful consideration is given to information provision and flows within the governance framework.

The Group Company Secretary has commenced work with Board Intelligence Limited to look at refreshing the Board and Committee paper templates, and the CEO report. As part of this, refresher training to paper authors on best practice paper writing to support the provision of high-quality information and effective decision making will be arranged. This exercise will involve reinforcing the use of best practice paper templates, which seek to help focus the Board on what matters (including checks against its Section 172 duties).

During the year, the Company dashboard (displaying key performance data and rapid insights on the overall health of the Group) was reviewed and redeveloped to streamline reporting across the Group. Board information continues to be distributed digitally, instantly and securely via the Board Intelligence platform once available. The Group Company Secretary is responsible to the Board for the timeliness and quality of information. All Directors have access to the advice and services of the Group Company Secretary.

Conflicts of interest

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

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

Shareholders

The Company's ultimate parent undertaking, Scotia Gas Networks Limited has three supportive shareholders. The Board interacts with the shareholder members on a regular basis and always acts fairly with members of the Company.

Board Meetings

There were six scheduled meetings of the Board in the year and two further Board calls in line with the agreed plan of business for the year, and details of Director attendance can be found on page 55-56.

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

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Board engagement out of the Boardroom

The Board also ensures it spends time out of the Boardroom with stakeholders. During the year the Board undertook site visits and employee engagement sessions with a number of employees. The Board plans to resume stakeholder engagement sessions going forward.

Board activity

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

The Board has also spent a significant time considering its strategy over the next five years with dedicated strategy sessions. As part of this, the Board has overseen a number of other strategy-related analyses, including, but not limited to: a review of the Group's pathway to the decarbonisation of heat, covering relevant trends in policy, technology, customer and stakeholder expectations; the Group's long-term financial outlook; assessment and prioritisation of growth opportunities; and a review of key risks.

Further details of the areas which have shaped the Board and Committee agendas during 2022/23 are set out below:

Board Focus	Detailed description
--------------------	-----------------------------

Strategy	
-----------------	--

- | | |
|--|--|
| | <ul style="list-style-type: none">- Supplier of Last Resort (SoLR), Third-Party Finance & Tariffs: consideration and approval of the SoLR and third-party finance strategy, and tariffs.
- Regulatory: consideration and approval of the Company's response to the Utility Regulator's (Northern Ireland) draft determination and received outcomes of the GD23 final determination.
- Customers: received and provided feedback on progress against the customer strategy and RIIO - GD2 customer experience programme to ensure RIIO - GD2 business plan requirements are met and maintain positive customer experience.
- Cyber Security & IT Resilience: continued to review IT resilience across the business and approved the ransomware policy.
- Energy Futures: reviewed the Energy Futures strategy covering the strategic framework, non-regulated activities, delivery of the strategy and future developments.
- ESG Reporting Framework: received an overview of ESG disclosures forming part of the World Economic Forum's Stakeholder Capitalism Metrics adopted by the Company's as the ESG reporting framework. |
|--|--|

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Directors' Report
for the Year Ended 31 March 2023

Board Focus Detailed description (cont.)
(cont.)

Performance

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

Governance

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Board Committees

The Board Committees convene to steer and supervise the SGN Group across strategy, performance and governance in the short, medium and long-term. As Southern Gas Networks plc and Scotland Gas Network plc are the main trading entities of the SGN Group, a significant amount of the Board Committees focus is directed towards these Companies. The Committee's SGN Midco group-related activities are introduced below.

Audit Committee

Membership

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

Attendees

The External Auditors are invited to attend the Audit Committee along with the Chief Financial Officer, the Head of Internal Audit, Risk and Compliance, the Finance Director and the Head of Financial Reporting and Tax, who represent Management.

The role of the Committee and principal responsibilities

The Audit Committee is a sub-committee of the Board. The Committee's role is to support the Board within the Governance Framework in matters relating to the:

- integrity of Financial Reporting;
- relationship with the External Auditor and the effectiveness of the external audit process;
- effectiveness of the Internal Audit and Compliance function; and
- effectiveness of the System of Internal Control.

The Audit Committee also reviews key regulatory filings prior to submission to Ofgem.

What the Committee has done this year

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

Key highlights

The key highlights for the year were:

Financial reporting

- Reviewed and considered key accounting judgements, the interim and final financial results and recommended the same for approval by the Board for the annual results for the statutory and regulatory accounts.
- Reviewed and approved the goodwill impairment and carrying value judgements.
- Reviewed the accounting treatment and provisions for key commercial projects.
- Received and discussed the key outcomes from the Financial Reporting Council's review of the Annual Report and Accounts for the year ending 31 March 2022.

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Directors' Report
for the Year Ended 31 March 2023

External audit

- Monitored the independence of the External Auditor.
- Reviewed the effectiveness of the external audit process and considered market trends and impacts.
- Considered the accounting, financial control and audit issues from the External Auditor's report.

Internal audit

- Reviewed the outputs from the external quality assessment undertaken on the Internal Audit function.
- Approved the annual audit plan and received regular updates on the delivery of the plan.

Risk management and internal controls

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

Regulatory filings and governance

- Approved the Debt to RAV and compliance certificates for Scotland Gas Network plc & Southern Gas Networks plc.
- Approved the financial compliance certificates for the MidCo Group.
- Monitored the level of non-audit fees and approved any new non-audit services.
- Reviewed the Data Assurance Guidelines for the Group.
- Reviewed the Prompt Payment Code return for the Group.

Looking forward

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

Finance Committee

Membership

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

Attendees

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

The role of the Committee and principal responsibilities

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

- distribution proposals and strategy including forecast distributions;
- financing and refinancing strategy and proposed debt issuance;
- financial risk management strategy;
- credit rating strategy;
- policies for the operation of bank accounts and facilities, including appointment of authorised personnel to those accounts and facilities; and
- policies for granting guarantees, indemnities, any type of parent-company support or security interest.

In addition, the Finance Committee will review and approve investments or transactions where the Finance Committee has been delegated authority by the Board to do so.

What the Committee has done this year

The Finance Committee held six meetings during the financial year of which three were additional to the planned. The Chair reports on key matters discussed to the Board and, where required, recommends decisions to be ratified by the Board in line with the Committee Terms of Reference.

Key highlights

The key highlights for the year were:

Strategy

- Reviewed and approved the EMTN programme base prospectus and associated transaction documents.
- Considered and approved new financing and risk management strategies for the Group's near-term refinancing requirements.
- Reviewed and approved a strategy to manage the mandatory break in one of Scotland's interest rate swaps.
- Approved the commissioning of a capital restructure analysis.

Governance

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

Looking forward

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Remuneration Committee

Membership

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

Attendees

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

The role of the Committee and principal responsibilities

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

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

What the Committee has done this year

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

Key highlights

The key highlights for the year were:

Strategy

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

Performance

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

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Directors' Report
for the Year Ended 31 March 2023

Governance

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

Looking forward

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

Health and Safety Committee

Membership

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

Attendees

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

The role of the Committee and principal responsibilities

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

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

What the Committee has done this year

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

SGN Midco Limited (Registered number: 11050000)

Directors' Report
for the Year Ended 31 March 2023

Key highlights

The key highlights for the year were:

Strategy

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

Performance

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

Governance

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

Looking forward

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

Stakeholder, Environment, Social and Governance Committee

Membership

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

Attendees

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

The role of the Committee and principal responsibilities

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

- Cultural, environmental, social and governance (ESG) issues;
- all stakeholders with an interest or concern in the Company; and
- the Company's impact (including the impact of any principal decisions taken by the Group) on the broader community and environment.

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

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What the Committee has done this year

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

Key highlights

The key highlights for the year were:

Strategy

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

Performance

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

Governance

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

Looking forward

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

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Directors' Report
for the Year Ended 31 March 2023

Nomination Committee

Membership

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

Attendees

The Chief Executive Officer and the HR & Services Director also attend the Nomination Committee meetings to represent Management.

The role of the Committee and principal responsibilities

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

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

All decisions are recommended to the Board for approval.

What the Committee has done this year

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

Key highlights

The key highlights for the year were:

Governance

- Formation of the Nomination Committee.
- Approved the appointment of the new Finance Committee Chair (Michael Botha).
- Approved the appointment of Jeff Rosenthal as Director and Felipe Ortiz and Antoine Kerrenneur as Alternate Directors to the Board.
- Reviewed the independence and approved the reappointment of the Sufficiently Independent Directors for Southern Gas Networks PLC and Scotland Gas Networks PLC as required under Standard Special Condition A42 of the Gas Transporters Licence and provision 10 of the Corporate Governance Code 2018.
- Reviewed and agreed changes to the Committee terms of reference.

Looking forward

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

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Directors' Report
for the Year Ended 31 March 2023

ATTENDANCE AT BOARD AND BOARD COMMITTEE MEETINGS

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

	Board meetings	Audit Committee meetings	Finance Committee meetings	Health and Safety Committee meetings
Directors				
Charlotte Brunning	6/6	-	6/6	-
Michael Botha	6/6	3/3	6/6	-
Martin Catchpole	6/6	3/3	6/6	-
Christian Fingerle	6/6	-	-	-
Paul Jeffery	6/6	3/3	6/6	-
Rebecca Lumlock	6/6	-	-	3/3
Felipe Ortiz*	3/3	-	-	-
Jeff Rosenthal*	3/3	-	-	-
Nicholas Salmon	6/6	3/3	-	3/3
Laura Sandys	6/6	-	-	3/3
Paul Trimmer	6/6	-	-	3/3

Notes to the tables above:

* - Jeff Rosenthal (previously Alternate Director) was appointed as a Director and Felipe Ortiz (previously Director) was appointed as Alternate Director on 24 November 2022.

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Directors' Report
for the Year Ended 31 March 2023

ATTENDANCE AT BOARD AND BOARD COMMITTEE MEETINGS - continued

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

Notes to the table above:

* - Jeff Rosenthal (previously Alternate Director) was appointed as a Director and Felipe Ortiz (previously Director) was appointed as Alternate Director on 24 November 2022.

** - Please find details regarding the membership of the Nomination Committee on Page 54.

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Directors' Report
for the Year Ended 31 March 2023

SGN Board Roles and Responsibilities

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

Chair

Responsible for leading the effective operation and governance of the Board:

- Setting agendas which support efficient and balanced decision-making
- Ensuring effective Board relationships and a culture that supports constructive discussion, challenge and debate
- Ensuring Board members are aware of and understand the views of key stakeholders
- Creating the conditions for overall Board effectiveness

Chief Executive Officer

Responsible for proposing and directing the delivery of strategy as agreed by the Board:

- Leadership and day-to-day management of the Group and Executive Committee
- Engaging with SGN's six key stakeholder groups and leading on related activity

Chief Financial Officer

Responsible for:

- The financial performance of the Group and supporting the Chief Executive Officer in implementing strategy
- Proposing policy and actions to support sound financial management
- Leading on unregulated activities
- Overseeing relationships with debt investors

Non-executive Shareholder Directors

Responsible for:

- Providing constructive challenge to the Board's decision-making processes
- Scrutinising, measuring and reviewing the performance of the Group
- Constructively challenging and assisting in the development of strategy
- Reviewing and challenging the performance of the Group's business against stakeholder interest

Independent Non-executive Directors

Responsible for the same responsibilities as Non-Executive Shareholder Directors, with the addition of:

- Bringing independence to the Board and its decision-making process
- Providing independent insight and support based on relevant experience
- Assessing risk and the integrity of the financial information and controls
- Providing independent input into the Group's strategy to reflect stakeholder interests

Company Secretary

Responsible for:

- Compliance with Board procedures and supporting the Chair
- Ensuring the Board has high quality information, adequate time and the appropriate resources
- Advising and keeping the Board updated on corporate governance developments
- Considering Board effectiveness in conjunction with the Chair
- Facilitating the Directors' induction programmes and training
- Providing advice, services and support to all Directors as and when required

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Directors' Report
for the Year Ended 31 March 2023

Directors' and Senior Executives' Biographies and Responsibilities as at 31 March 2023

Nick Salmon, Chair, Non-executive Director

Nick joined the Board in March 2019 and was appointed the Chair of SGN in March 2021. He is also the Chair of Pressure Technologies plc. Previously he was Chair to South East Water Ltd, the Senior Independent Director at both United Utilities plc and Elementis plc, a non-executive Director at Interserve plc and CEO of Cookson Group plc and Babcock International Group plc. Nick is member of the Audit Committee and is the Chair of the Health and Safety Committee and Nomination Committee.

Charlotte Brunning, Non-executive Director

Charlotte joined the Board in May 2018. She is a member of the EMEA Infrastructure and Natural Resources team and had been with Ontario Teachers' since 2015. She has been involved in a number of direct investments, including London City Airport, ADNOC, SGI and SGN Smart. Charlotte holds a B.Sc. from the London School of Economics and an MBA from the London Business School. Charlotte is also director of Galaxy Pipeline Assets Holdco Limited, Apple Newco Limited, SGI and Scottish Hydro Electric Transmission plc. Charlotte serves as the Chair of the Remuneration Committee. She is also member of the Finance Committee, Nomination Committee and the Stakeholder, Environment, Social and Governance Committee.

Martin Catchpole, Non-executive Director

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

Paul Trimmer, Non-executive Director

Paul joined the Board in March 2022 and is a Senior Advisor to Global Infrastructure Partners ('GIP') focusing on its energy sector. He has been a Board Director of FluxSwiss, CLH-PS and Interconnector UK and is an Advisory Board Member for Carbon Connect (an entity supporting the UK's transition to Net Zero). Previously, Paul spent 32 years in Shell, including as an Executive Director of Comgas and Transredes. Paul is also a Partner in Atosú. Paul is member of the Remuneration Committee, Nomination Committee, the Health and Safety Committee and the Stakeholder, Environment, Social and Governance Committee.

Michael Botha, Non-executive Director

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

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Rebecca Lumlock, Non-executive Director

Rebecca joined the Board in March 2022 and is an Operating Partner in Brookfield. She is also currently Interim CEO of Freightliner, the UK rail freight company. Prior to this she worked for Network Rail for five years including as the Managing Director for the Wessex Route, including London Waterloo. She was also their Group executive sponsor for gender. Becky has worked in the oil and gas industry for over 20 years across four continents, most recently as Managing Director of Dragon LNG, importing liquefied natural gas from around the world to help satisfy the UK's gas demand. Rebecca is also director of UK Gas Distribution 2 Limited, Galaxy Pipeline Assets Holdco Limited and PD Ports Limited. Rebecca is member of the Remuneration Committee, Nomination Committee, the Health and Safety Committee and the Stakeholder, Environment, Social and Governance Committee.

Felipe Ortiz, Non-executive Director

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

Christian Fingerle, Non-executive Director

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

Charles Thomazi, Alternate Director

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

Michael Smart, Alternate Director

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

Jeff Rosenthal, Alternate Director

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

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Directors' Report
for the Year Ended 31 March 2023

Antoine Kerrenneur, Alternate Director

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

Paul Jeffery, Statutory Independent Non-executive Director

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

Laura Sandys, Statutory Independent Non-executive Director

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

Mark Wild OBE, Chief Executive Officer

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

Mick Carmedy, Chief Financial Officer

Mick joined the Company in January 2018. Mick was CFO of Southern Water, the regulated water business, for five years prior to joining. Mick has also worked at United Utilities and Thames Water in a variety of financial, commercial and regulatory roles.

Nicola Shand, Chief of Staff and Director of Legal Services, Group Company Secretary

Nicola joined the Board as Company Secretary in July 2011. Nicola is the Chief of Staff and Director of Legal Services for SGN. Nicola is responsible to the Board for compliance with Board procedures and for advising and keeping the Board up to date on all corporate governance developments.

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Directors' Report
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STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITORS

So far as the directors are aware, there is no relevant audit information (as defined by Section 418 of the Companies Act 2006) of which the group's auditor is unaware, and each director has taken all the steps that he or she ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that the group's auditor is aware of that information.

AUDITOR

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

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

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

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

BY ORDER OF THE BOARD:

DocuSigned by:

812D87E00D78481
Nicola Shand - Secretary

Date: 27-07-23 | 4:15 AM PDT
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SGN Midco Limited (Registered number: 11050000)

Directors' Responsibilities Statement
for the Year Ended 31 March 2023

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

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

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

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

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

Independent Auditor's Report to the Members of
SGN Midco Limited

Opinion

We have audited the financial statements of SGN Midco Limited ('the parent company') and its subsidiaries (the 'group') for the year ended 31 March 2023 which comprise the Consolidated Profit and Loss Account, the Consolidated Statement of Comprehensive Income, the Consolidated Balance Sheet, the Company Balance Sheet, the Consolidated Statement of Changes in Equity, the Company Statement of Changes in Equity, the Consolidated Cashflow Statement and the related notes 1 to 34, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

- give a true and fair view of the group's and of the parent company's affairs as at 31 March 2023 and of the group's profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

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

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

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the group and parent company's ability to continue as a going concern for a period of twelve months (to 31 July 2024) from when the financial statements are authorised for issue.

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

Independent Auditor's Report to the Members of
SGN Midco Limited

Other information

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

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

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

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

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

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

Matters on which we are required to report by exception

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

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

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

Independent Auditor's Report to the Members of
SGN Midco Limited

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.

Auditor's responsibilities for the audit of the financial statements

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

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

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

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the company and determined that the most significant are those that relate to the reporting framework (FRS 102 and the Companies Act 2006) and the local tax legislation.
- We understood how the Group is complying with those frameworks by making enquiries of management, internal audit and those responsible for legal and compliance procedures and the Company secretary. We corroborated our enquiries through our review of Board minutes, papers provided to the Group's Audit Committee and correspondence received from regulatory bodies and noted that there was no contradictory evidence.

Independent Auditor's Report to the Members of
SGN Midco Limited

- We assessed the susceptibility of the Company's financial statements to material misstatement, including how fraud might occur by meeting with management from various parts of the business to understand where it considered there was susceptibility to fraud. We considered the programmes and controls that the Group has established to address risks identified, or that otherwise prevent, deter and detect fraud; and how senior management monitors those programmes and controls. Where the risk was considered to be higher, we performed audit procedures to address each identified fraud risk. These procedures included using data analysis for testing journal entries that met our defined risk criteria based on our understanding of the business and challenging the assumptions and judgements made by management in areas where judgement is required.

- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved understanding management's internal controls over compliance with laws and regulations; enquiry of legal counsel, management and internal audit; and reviewing internal audit reports and whistleblowing logs.

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

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.

DocuSigned by:
Ernst & Young LLP
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Steve Dobson (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
Date: 27-07-23 | 5:28 PM BST

SGN Midco Limited (Registered number: 11050000)Consolidated Profit and Loss Account
for the Year Ended 31 March 2023

	Notes	2023 £m	2022 £m
TURNOVER¹	3	1,244	1,060
Net operating costs ²		<u>(793)</u>	<u>(719)</u>
OPERATING PROFIT		451	341
Interest receivable and similar income	5	17	7
Interest payable and similar expenses	6	(274)	(195)
Fair value movement on derivatives	11	<u>(1)</u>	<u>(73)</u>
PROFIT BEFORE TAXATION	7	193	80
Tax on profit	8	<u>(50)</u>	<u>(260)</u>
PROFIT/(LOSS) FOR THE FINANCIAL YEAR		<u>143</u>	<u>(180)</u>
Profit/(loss) attributable to: Owners of the parent		<u>143</u>	<u>(180)</u>

¹Included within Turnover are exceptional items to the sum of £31m (2022: £nil), see note 11 for more details.

²Included within Net operating costs are exceptional items to the sum of £nil (2022: £31m), see note 11 for more details.

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

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)Consolidated Statement of Comprehensive Income
for the Year Ended 31 March 2023

	Notes	2023 £m	2022 £m
PROFIT/(LOSS) FOR THE YEAR		143	(180)
OTHER COMPREHENSIVE (LOSS)/INCOME			
Profit arising on cash flow hedge	8	21	16
Remeasurement on net pension asset	8	(117)	57
Income tax relating to components of other comprehensive income	8	<u>24</u>	<u>(19)</u>
OTHER COMPREHENSIVE (LOSS)/INCOME FOR THE YEAR, NET OF INCOME TAX		<u>(72)</u>	<u>54</u>
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR		<u><u>71</u></u>	<u><u>(126)</u></u>
Total comprehensive income/(loss) attributable to: Owners of the parent		<u><u>71</u></u>	<u><u>(126)</u></u>

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)Consolidated Balance Sheet31 March 2023

	Notes	2023 £m	2022 £m
FIXED ASSETS			
Intangible assets	13	334	348
Tangible assets	14	7,232	7,021
Non-current financial assets	12	<u>5</u>	<u>-</u>
		<u>7,571</u>	<u>7,369</u>
CURRENT ASSETS			
Debtors: amounts falling due within one year	16	161	114
Short term deposits	17	210	55
Cash at bank	18	<u>43</u>	<u>25</u>
		414	194
CREDITORS			
Amounts falling due within one year	19	(658)	(583)
NET CURRENT LIABILITIES		<u>(244)</u>	<u>(389)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		7,327	6,980
CREDITORS			
Amounts falling due after more than one year	20	(4,856)	(4,659)
PROVISIONS FOR LIABILITIES	23	(1,102)	(1,092)
DEFERRED INCOME	24	(483)	(461)
PENSION ASSET	27	<u>246</u>	<u>363</u>
NET ASSETS		<u>1,132</u>	<u>1,131</u>

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)Consolidated Balance Sheet - continued
31 March 2023

	Notes	2023 £m	2022 £m
CAPITAL AND RESERVES			
Called up share capital	25	28	28
Hedging reserves	26	(25)	(41)
Merger reserve	26	(2,787)	(2,787)
Profit and loss account	26	<u>3,916</u>	<u>3,931</u>
SHAREHOLDERS' FUNDS		<u>1,132</u>	<u>1,131</u>

The financial statements were approved by the Board of Directors and authorised for issue on 27-07-23 | 11:54 AM BST and were signed on its behalf by:

DocuSigned by:

Nick Salmon

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Nicholas Robin Salmon (Chair) - Director

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)Company Balance Sheet31 March 2023

	Notes	2023 £m	2022 £m
FIXED ASSETS			
Investments	15	<u>2,815</u>	<u>2,815</u>
		<u>2,815</u>	<u>2,815</u>
CURRENT ASSETS			
Debtors: amounts falling due within one year	16	46	44
Short term deposits	17	<u>4</u>	<u>9</u>
		50	53
CREDITORS			
Amounts falling due within one year	19	<u>-</u>	<u>(1)</u>
NET CURRENT ASSETS		<u>50</u>	<u>52</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		2,865	2,867
CREDITORS			
Amounts falling due after more than one year	20	<u>(459)</u>	<u>(440)</u>
NET ASSETS		<u>2,406</u>	<u>2,427</u>
CAPITAL AND RESERVES			
Called up share capital	25	28	28
Profit and loss account	26	<u>2,378</u>	<u>2,399</u>
SHAREHOLDERS' FUNDS		<u>2,406</u>	<u>2,427</u>
Company's profit for the financial year		<u>49</u>	<u>99</u>

The financial statements were approved by the Board of Directors and authorised for issue on 27-07-23 | 11:54 AM BST and were signed on its behalf by:

DocuSigned by:

Nick Salmon

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Nicholas Robin Salmon (Chair) - Director

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)**Consolidated Statement of Changes in Equity
for the Year Ended 31 March 2023**

	Called up share capital £m	Profit and loss account £m	Hedging reserves £m	Merger reserve £m	Total equity £m
Balance at 1 April 2021	28	4,177	(57)	(2,787)	1,361
Loss for the year	-	(180)	-	-	(180)
Other comprehensive income	-	38	16	-	54
Total comprehensive (loss)/ income	-	(142)	16	-	(126)
Dividends	-	(104)	-	-	(104)
Transactions with owners, recognised directly in equity	-	(104)	-	-	(104)
Balance at 31 March 2022	28	3,931	(41)	(2,787)	1,131
Profit for the year	-	143	-	-	143
Other comprehensive (loss)/ income	-	(88)	16	-	(72)
Total comprehensive income	-	55	16	-	71
Dividends	-	(70)	-	-	(70)
Transactions with owners, recognised directly in equity	-	(70)	-	-	(70)
Balance at 31 March 2023	28	3,916	(25)	(2,787)	1,132

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)Company Statement of Changes in Equity
for the Year Ended 31 March 2023

	Called up share capital £m	Profit and loss account £m	Total equity £m
Balance at 1 April 2021	28	2,404	2,432
Changes in equity			
Profit for the year	-	99	99
Total comprehensive income	-	99	99
Dividends	-	(104)	(104)
Transactions with owners, recognised directly in equity	-	(104)	(104)
Balance at 31 March 2022	28	2,399	2,427
Changes in equity			
Profit for the year	-	49	49
Total comprehensive income	-	49	49
Dividends	-	(70)	(70)
Transactions with owners, recognised directly in equity	-	(70)	(70)
Balance at 31 March 2023	28	2,378	2,406

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)**Consolidated Cash Flow Statement**
for the Year Ended 31 March 2023

	Notes	2023 £m	2022 £m
Cash flows from operating activities			
Cash generated from operations	31	698	548
Interest paid	33	(157)	(145)
Tax paid		<u>(41)</u>	<u>(38)</u>
Net cash from operating activities		<u>500</u>	<u>365</u>
Cash flows from investing activities			
Purchase of intangible fixed assets		(9)	(8)
Purchase of tangible fixed assets		(394)	(338)
Sale of tangible fixed assets		1	-
Customer contributions received		33	37
Interest received		<u>2</u>	<u>-</u>
Net cash used in investing activities		<u>(367)</u>	<u>(309)</u>
Cash flows from financing activities			
Issue of debt		399	30
Repayment of debt		(308)	(122)
Payments of mirror swaps	33	-	(28)
Payments of interest rate swaps		(3)	(4)
Receipts from inflation-linked swaps		22	13
Dividends paid		<u>(70)</u>	<u>(104)</u>
Net cash from/ (used in) financing activities		<u>40</u>	<u>(215)</u>
Increase/(decrease) in cash and cash equivalents		<u>173</u>	<u>(159)</u>
Cash and cash equivalents at beginning of year	32	<u>80</u>	<u>239</u>
Cash and cash equivalents at end of year	32	<u><u>253</u></u>	<u><u>80</u></u>

The notes on pages 75 to 127 form part of these financial statements

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES

General information and basis of preparation

SGN MidCo Limited is a private company limited by shares and is incorporated in England and Wales under the Companies Act 2006. The address of the registered office is St Lawrence House, Station Approach, Horley, Surrey, RH6 9HJ, United Kingdom. The company's principal activity is that of an intermediate holding company within the Scotia Gas Networks Group comprising SGN MidCo Limited and its subsidiaries.

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

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

The functional currency of the Group is pound sterling because that is the currency of the primary economic environment in which the Group operates. Amounts are expressed in millions of pounds except where noted otherwise.

The Company is a wholly owned subsidiary of SGN PledgeCo Limited which in turn is a wholly owned subsidiary of Scotia Gas Networks Limited and the financial statements of the Company are included in the consolidated financial statements of Scotia Gas Networks Limited which can be obtained from the address above.

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

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

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

The following principal accounting policies have been applied:

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES – continued

Going concern

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

The directors have forecast cash flows of the Group for the next twelve months to 31 July 2024 (the going concern period) and have obtained a support letter from Scotia Gas Networks Limited confirming that it can and will support the Company in meeting its liabilities throughout the going concern period.

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

Consequently, the Directors believe that the Group will be able to meet its liabilities as they fall due and will have adequate resources to continue in operational existence for the going concern period, being twelve months (to 31 July 2024) from the date of approval of this report. Accordingly, the Directors continue to adopt the going concern basis in preparing the financial statements.

Turnover

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

Intangible assets - goodwill

Goodwill arising on the acquisition of businesses, representing any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and amortised on a straight-line basis over its useful economic life, which is estimated to be 50 years. Impairment indicators for goodwill are assessed on an annual basis at each balance sheet date in line with FRS 102 requirements.

Intangible assets - software

Software assets are included at cost, net of amortisation and any provision for impairment. Amortisation is provided on a straight-line basis over their estimated useful economic life of 3 to 10 years. The Group's intangible assets have a remaining useful economic life ranging between 1 - 5 years.

Tangible fixed assets

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

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

Freehold buildings:	Up to 50 years
Leasehold land and buildings:	Over the shorter of lease term and 50 years
Plant and machinery:	
-Mains and services:	55 to 65 years
-Regulating equipment:	30 to 50 years
-Gas storage:	40 years
-Motor vehicles and office equipment:	3 to 10 years

Site remediation costs are depreciated over the life of the asset.

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

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

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

Fixed Asset Investments

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

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

Financial instruments

FRS 102 sections 11 and 12 give an accounting policy choice for financial instruments. The Group has chosen to apply the recognition and measurement provisions of IAS 39 and the disclosure requirements of FRS 102 in respect of financial instruments.

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

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

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

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

i. Effective interest method

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

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

ii. Financial Assets

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

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES – continued

iii. Impairment of financial assets

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

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

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

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

iv. Derecognition of financial assets

The 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.

v. Trade debtors

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

vi. Cash

Cash comprises cash on hand and demand deposits, which are those deposits, which are repayable on demand and available within 24 hours (one day) without penalty. The Group receives monies in the form of grants and contributions towards innovation projects. The use of this cash is restricted by the specific terms and conditions of each project.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

vii. Financial liabilities

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

viii. Financial liabilities at FVTPL

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

A financial liability is classified as held for trading if:

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

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

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

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

ix. Other financial liabilities

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

x. De-recognition of financial liabilities

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

xi. Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments for risk management purposes.

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

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

On inception of the hedge relationship the Group documents the relationships between the hedged item and the hedging instrument along with the risk management objectives and its strategy for undertaking various transactions. Furthermore, at inception of the hedge and on an ongoing basis the Group documents whether the hedging relationship is highly effective. The Group also uses inflation-linked swaps to hedge the risk arising from its inflation-linked asset base and revenues, which do not qualify for hedge accounting treatment.

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

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

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

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES – continued

Taxation

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

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date.

Timing differences are differences between the Group's taxable profits and its results as stated in the financial statements that arises from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date that are expected to apply to the reversal of the timing difference.

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

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

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

The Group uses inflation-linked swaps to hedge its inflation-linked regulated asset base and turnover, which do not qualify for hedge accounting treatment however the fair value movements on these financial instruments are disregarded for tax purposes.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. **ACCOUNTING POLICIES - continued**

Employee benefits

i. Defined benefit pension scheme

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

For defined benefit schemes the amounts charged to operating profit are the costs arising from employee services rendered during the year and the cost of plan introductions, benefit changes, settlements and curtailments. They are included as part of staff costs. The net interest cost on the net defined benefit liability is charged to profit or loss and included within finance costs.

Remeasurement comprising actuarial gains and losses and the return on scheme assets (excluding amounts included in net interest on the net defined benefit liability) are recognised immediately in other comprehensive income.

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

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

ii. Defined contribution pension scheme

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

Impairment of non-financial assets

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

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

Goodwill impairment

The recoverable amount of goodwill is the higher of the value in use or the fair value less cost to dispose. This is derived from measurement of the present value of the future cash flows of the business. Any impairment loss is allocated first to the goodwill, and then to other assets on a pro-rata basis. The Company considers there to be two separate CGUs for the purpose of goodwill impairment: Southern Gas Networks plc and Scotland Gas Networks plc.

Other non-financial assets

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

Operating leases

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

Borrowing costs capitalised

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

Grants and contributions

1) Customer contributions

Customer contributions for connections to the network and for replacement expenditure diversions are treated as capital grants. They are accounted for as deferred income (creditors due after more than one year) and released to profit and loss on a straight-line basis over the estimated life of the related asset. The corresponding asset is capitalised within fixed assets and is depreciated over its useful economic life. Customer contributions which have been received by the end of the financial year, for which the corresponding asset has not yet been delivered are treated as creditors due within one year.

2) Government grants

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are discounted where the impact of discounting the expected future cash flows is material. No provision is required for the repair of gas pipes as these are replaced on an agreed basis with the Regulator.

Contingent liabilities

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

Short term deposits

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

Interest receivable and Interest payable

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

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

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

Dividends

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

1. ACCOUNTING POLICIES - continued

Exceptional items

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

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

Fair value movements on derivatives

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

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

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

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

Critical accounting judgements

- a** Cost classification - The Group incur significant staff and contractor costs for fulfilling normal business activities. Management judgement is required to allocate costs between capital, replacement and operating expenditure depending on the nature of the work being performed. Capital and replacement expenditure as reported in the Strategic Report on page 31 and 32 are both recognised as additions to plant and equipment within tangible fixed assets. Operating expenditure is recognised within Net operating costs within the Profit and Loss account.
- b** Impairment of fixed assets - as set out in note 1 above, management has exercised judgement during the group balance sheet review when identifying impairment indicators affecting the fixed assets of the Group and the goodwill on the cost generating units (CGUs).

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY
– continued

- c Exceptional items - The categorisation of certain items as exceptional follows a three-step process which considers the nature of the event, materiality involved and any particular facts and circumstances. Management focuses on whether the event is considered to be one-off in nature. See note 11.
- d Supplier of last resort - Management have given consideration to the Supplier of Last Resort (SoLR) mechanism under the Group's regulatory transportation licenses. The Group accounts for SoLR payments as levies, and as such will only be obliged to pay the costs when reciprocating incremental levies are received. In relation to the SoLR mechanism, the Group does not hold inventory risk, does not set the SoLR mechanism pricing and is not exposed to credit risk. As such, it is management's judgment that the Group is acting as an Agent and therefore associated revenues and costs are not shown within Turnover or Net operating costs within the Consolidated Profit and Loss account. The SOLR mechanism's only impact on the current and prior year financial statements is an immaterial balance originating from timing differences in payment and recovery, which is recorded in other creditors on the Consolidated Balance sheet.
- e Customer contributions - Cash inflows are presented as cash flows from investing activities in the Consolidated cash flow statement, as customer contributions are directly associated with capital investment in the Group's gas networks.
- f Galpin's Road Investigation – Management judgement is required in assessing if the recognition criteria for a provision has been met in relation to the Galpin's Road incident as at 31 March 2023 (as described on page 4).

Based on external legal advice, management has concluded that the investigation is not sufficiently progressed to reliably estimate the financial impact or timing of any future obligation. As such the case has been disclosed as a contingent liability (see note 28) until the point at which any economic transfer can be reliably estimated.

Key source of estimation uncertainty

- a Useful lives of assets - The Group depreciates its assets over their useful economic lives. The estimation of the useful lives of assets is based on historic performance as well as expectations about future use and therefore requires estimates and assumptions to be applied by management. The useful economic lives of assets can vary depending on a variety of factors, including technological innovation, climate change and climate related impacts, product life cycles, maintenance programmes as well as the economic life of the gas industry. The depreciation policy is set out in note 1.
- b Retirement benefit schemes - the assumptions used in accounting for the defined benefit pension scheme are based on estimates and are subject to uncertainties. These assumptions are set out in note 26 and include: the discount rate on scheme liabilities, mortality rates, pension increases, salary increases and inflation. The Company takes advice from independent actuaries on the appropriateness of these assumptions.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY – continued

- c Valuation of financial instruments - where financial instruments are recognised at fair value there are uncertainties in forward yield curves used in discounted cash flow calculations.
- d Environmental provision - in assessing the degree of contamination at the various sites, estimation is required where elements of the contamination are underground. In these cases, it is difficult to assess with any certainty the extent of the contamination. The discount rate is also a source of estimation.
- e Climate change- In assessing the impact of climate change on the Group, management have considered two key areas being useful economic life and impairment of fixed assets. Management believes the role of hydrogen in the UK's energy transition will support both the UEL of the networks and the recoverable amount of the respective CGU's. Therefore, the Group assesses that there is currently limited exposure to climate related risks.
- f Operational target provision - During the year, the Group failed to meet the 97% target imposed by the Gas Transporter Standard Special Conditions D10 in relation to the time taken to respond to gas escapes. As at 31 March 2023 management considers the recognition criteria for a provision to have been met, as there is a probable future economic transfer resulting from the missed target.

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

3. TURNOVER

The Board and Chief operating decision maker view the Group as one operating segment.

Analysis of turnover by class of business:

	2023	2022
	£m	£m
Transportation of natural gas and the provision of related services	1,244	1,060

All turnover arose in the United Kingdom.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

4. EMPLOYEES AND DIRECTORS

The Group had 4,012 full-time equivalent employees as at 31 March 2023 (2022: 3,638). The average monthly number of full-time equivalent employees during the year was 3,816 (2022: 3,648).

	2023	2022
Field based staff	2,139	1,958
Office and other administrative staff	1,873	1,680
	<u>4,012</u>	<u>3,638</u>

The Independent Directors received remuneration totalling £201,528 (2022: £198,648) for their services to the Group during the year. No retirement benefits are accruing in the year or in the prior year to any Directors under money purchase or defined benefit schemes, in respect of their services to the Group. There are 11 directors who did not receive any remuneration in respect of services to the Group during the current or preceding financial year. These directors are employed by the SGN Group's shareholders and do not specifically receive any remuneration in respect of the company and the time spent working as a board member on SGN was deemed immaterial.

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

	2023	2022
	£m	£m
Wages and salaries	32	32
Social security costs	4	4
Pension costs (Note 27) ¹	31	31
	<u>67</u>	<u>67</u>

¹ Pension costs include the amount charged in respect of defined contributions schemes and the current service cost on the defined benefit scheme.

The SGN Midco Limited group utilises the services of employees contracted to a fellow Scotia Gas Networks Limited group company. The cost of these services recharged to the SGN Midco Limited group in the year is £131m (2022: £107m) which are included within Net operating costs in the Profit and Loss account but excluded from the table above.

5. INTEREST RECEIVABLE AND SIMILAR INCOME

	2023	2022
	£m	£m
Interest receivable on loans to other group undertakings	2	1
Net defined benefit pension income	10	6
Deposit account interest	2	-
Other interest receivable	3	-
	<u>17</u>	<u>7</u>

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

6. INTEREST PAYABLE AND SIMILAR EXPENSES

	2023	2022
	£m	£m
Interest payable on fixed rate instruments	121	107
Interest payable on floating rate instruments	7	3
Interest payable on inflation-linked instruments	131	74
Other interest payable	14	11
Unwinding of discount	1	-
	<u>274</u>	<u>195</u>

Included within interest payable on inflation-linked instruments is £133m of accretion on RPI-linked debt instruments (31 March 2022: £58m).

In June 2022, Southern Gas Networks plc agreed to settle outstanding fees due in relation to certain guarantees provided by Assured Guarantee Corp. (as agent for Syncora Guarantee Inc.) and Assured Guarantee UK Limited that were previously in place over certain outstanding public bond instruments. The cash settlement amount of £9m is included within the "interest paid" line of the cash flow statement.

In March 2022, the Group agreed to settle outstanding fees due in relation to certain guarantees provided by Ambac Assurance UK Limited that were previously in place over certain outstanding public bond instruments, but which were removed in November 2020. The cash settlement amount of £4m is included within the interest paid line of the cash flow statement for the comparative period.

7. PROFIT BEFORE TAXATION

The profit is stated after charging/(crediting):

	2023	2022
	£m	£m
Depreciation - owned assets	184	180
Loss on disposal of fixed assets	4	5
Goodwill amortisation	10	9
Computer software amortisation	13	12
Amortisation of customer contributions	(11)	(10)
Operating lease rentals	<u>4</u>	<u>3</u>

Auditor's remuneration for the Group comprises:

- Audit of these financial statements £11,261 (2022: £9,172)
- Audit of financial statements of subsidiaries of the company £372,823 (2022: £303,683)
- Audit-related assurance services £105,000 (2022: £99,200)
- Other assurance services £70,000 (2022: £37,200)

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****8. TAXATION****Analysis of the tax charge**

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

	2023 £m	2022 £m
Current tax:		
UK corporation tax	33	30
Prior year adjustment	(5)	-
Total current tax	28	30
Deferred tax:		
Origination and reversal of timing differences	8	(13)
Prior year adjustment	7	(3)
Effect of change in tax rate	7	246
Total deferred tax	22	230
Tax on profit	50	260

UK corporation tax has been charged at 19% (2022 - 19%).

Reconciliation of total tax charge included in profit and loss

The tax assessed for the year is higher than (2022: higher than) the standard rate of corporation tax in the UK. The difference is explained below:

	2023 £m	2022 £m
Profit before tax	193	80
Profit multiplied by the standard rate of corporation tax in the UK of 19% (2022 - 19%)	37	15
Effects of:		
Expenses not deductible for tax purposes	2	-
Adjustments to tax charge in respect of previous periods	2	(3)
Non-deductible goodwill	2	2
Effect of change in tax rate	7	246
Depreciation on non-qualifying assets	1	1
Permanent benefit of capital allowances super deduction	(1)	(1)
Total tax charge	50	260

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

8. TAXATION - continued

Tax effects relating to effects of other comprehensive income

		2023	
	Gross	Tax	Net
	£m	£m	£m
Profit arising on cash flow hedge	21	(5)	16
Remeasurement on net pension asset	(117)	29	(88)
	<u>(96)</u>	<u>24</u>	<u>(72)</u>
	Gross	2022	Net
	£m	Tax	£m
	£m	£m	£m
Profit/(loss) arising on cash flow hedge	16	-	16
Remeasurement on net pension asset	57	(19)	38
	<u>73</u>	<u>(19)</u>	<u>54</u>

The standard rate of tax applied to reported profit on ordinary activities is 19% (2022: 19%). Finance Act 2021 increased the main rate of corporation tax from 19% to 25% from 1 April 2023. As these changes have been substantively enacted at the at the comparative period's balance sheet date deferred tax has been calculated based on the rate that is expected to apply when the deferred tax is reversed, resulting in an increase to the company's deferred tax liability at 31 March 2023 by £7m (2022: £246m).

Movements in deferred tax take into account the effects of changes in the fair value liability of the Group's inflation-linked swap portfolio. Increases or reductions in the fair value liability of the Group's inflation linked swap portfolio represent an increase or reduction in the present value of the future cash flows that will be payable/receivable on those inflation-linked swaps in future years. Changes to the fair value of the liability are not tax deductible under UK tax regulations as tax deductions are only available as and when the interest payments/receipts are actually accrued. The increase in the fair value of the inflation-linked swap portfolio will therefore create an accounting cost which is not subject to taxation until the cash flow is accrued and therefore creates a timing difference. The fair value of the inflation-linked swap portfolio can fluctuate significantly and there will be a consequential impact on the deferred tax provision.

9. PROFIT OF THE COMPANY FOR THE FINANCIAL YEAR

As permitted by Section 408 of the Companies Act 2006, the Profit and Loss Account of the parent company is not presented as part of these financial statements. The Company's profit for the year amounted to £49m (2022: £99m).

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**10. DIVIDENDS**

Interim dividends paid for the year ended 31 March 2023 amount to £70m (2.48p per share) (2022: £104m (3.71p per share)). No further dividends were proposed.

The dividends paid in the current year of £70m were paid in November 2022.

11. EXCEPTIONAL ITEMS AND FAIR VALUE MOVEMENTS

	2023 £m	2022 £m
Exceptional items included within turnover:		
Incremental turnover from recovery of costs due to increase in gas wholesale prices*	(31)	-
Exceptional items included within Net operating costs:		
Cost impact of increase in gas wholesale prices*	-	31
Included within taxation:		
Tax charge/ (credit) on cost impact of increase in gas wholesale prices	6	(6)
Fair value movements:		
Net losses on derivative financial instruments**	1	73
Included within taxation:		
Tax charge/ (credit) on net losses on derivative financial instruments	4	(16)

*In the year, the Group recorded incremental turnover as a result of recovering incremental costs charged in the prior year of £31m (2022: nil) associated with the rise in wholesale gas prices through its regulated tariffs. These incremental costs were disclosed as exceptional items in the prior year and as such the associated income received in the current year is disclosed as such.

**Net losses on derivative financial instruments comprise gains and losses arising on derivative financial instruments reported in the Statement of Profit and Loss. These exclude gains and losses for which hedge accounting has been effective, which has been recognised directly in the consolidated statement of comprehensive income. There was nil impact (2022: £nil) to the cash flow as a result of the fair value movements on financial derivatives. Included within net losses on derivative financial instruments is £71m (2022: £36m) of accretion on CPI-linked swaps.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**12. NON-CURRENT FINANCIAL ASSETS****Group**

	2023 £m	2022 £m
Derivative financial instruments - interest rate swaps	<u>5</u>	<u>-</u>

13. INTANGIBLE FIXED ASSETS**Group**

	Goodwill £m	Computer software £m	Totals £m
COST			
At 1 April 2022	478	192	670
Additions	-	9	9
Disposals	<u>-</u>	<u>(106)</u>	<u>(106)</u>
At 31 March 2023	<u>478</u>	<u>95</u>	<u>573</u>
AMORTISATION			
At 1 April 2022	157	165	322
Amortisation for year	10	13	23
Eliminated on disposal	<u>-</u>	<u>(106)</u>	<u>(106)</u>
At 31 March 2023	<u>167</u>	<u>72</u>	<u>239</u>
NET BOOK VALUE			
At 31 March 2023	<u>311</u>	<u>23</u>	<u>334</u>
At 31 March 2022	<u>321</u>	<u>27</u>	<u>348</u>

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

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

	2023 £m	2022 £m
Southern Gas Networks plc	210	217
Scotland Gas Networks plc	<u>97</u>	<u>100</u>
	307	317

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****13. INTANGIBLE FIXED ASSETS – continued**

A review for impairment of goodwill is carried out when there are indicators of impairment. As at 31 March 2023, following management's assessment of internal and external impairment indicators, no such indicators were noted. As such no impairment charge has been recorded for the current year (2022: £nil).

The amortisation charge is recognised in Net operating costs in the profit and loss account. No impairment loss has been recorded in the current year or prior years.

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

During the year, the Group wrote off £106m of fully amortised assets, that are no longer in use, in line with the Group's accounting policy.

The Company has no intangible fixed assets.

14. TANGIBLE FIXED ASSETS**Group**

	Freehold property £m	Short leasehold £m	Plant and machinery £m	Computer equipment £m	Totals £m
COST					
At 1 April 2022	136	1	8,702	152	8,991
Additions	10	-	371	19	400
Disposals	-	-	(19)	(4)	(23)
At 31 March 2023	<u>146</u>	<u>1</u>	<u>9,054</u>	<u>167</u>	<u>9,368</u>
DEPRECIATION					
At 1 April 2022	51	-	1,820	99	1,970
Charge for year	6	-	167	11	184
Eliminated on disposal	-	-	(14)	(4)	(18)
At 31 March 2023	<u>57</u>	<u>-</u>	<u>1,973</u>	<u>106</u>	<u>2,136</u>
NET BOOK VALUE					
At 31 March 2023	<u>89</u>	<u>1</u>	<u>7,081</u>	<u>61</u>	<u>7,232</u>
At 31 March 2022	<u>85</u>	<u>1</u>	<u>6,882</u>	<u>53</u>	<u>7,021</u>

The Company has no tangible fixed assets.

Included within Freehold property is the Net book value of land of £9m (2022: £9m).

There is no security held against the tangible fixed assets of the Group.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**15. FIXED ASSET INVESTMENTS****Company**Shares in
group
undertakings
£m**COST**

At 1 April 2022 and 31 March 2023

2,815**NET BOOK VALUE**

At 31 March 2023

2,815

At 31 March 2022

2,815

The Group holds 23.02% (2022: 23.02%) of the ordinary shares of Xoserve Limited, the investment is held at carrying value of £0.2m (2022: £0.2m). Xoserve Limited provides transportation transactional services on behalf of all the major gas network transportation companies. The address of its registered office is Lansdowne Gate, 65 New Road, Solihull, B91 BDL. The Xoserve Limited operating results for the year ended 31 March 2023 are not considered material to the Group's financial statements.

Details of the subsidiary undertakings at the end of the year, which are directly wholly owned by the company, are as follows:

Name of subsidiary	Description of shares held	Country of registration	Principal activities
Southern Gas Networks plc	160,174,771 ordinary shares of £1 each	England & Wales	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services.
Scotland Gas Networks plc	49,392,787 ordinary shares of £1 each	Scotland	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services.
SGN Contracting Limited	1 ordinary share of £1	England & Wales	Dormant
SGN Natural Gas Limited	1 ordinary share of £1	England & Wales	Development, administration, maintenance and operation of regional gas distribution system and supply of transportation services.

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

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**16. DEBTORS: AMOUNTS FALLING DUE WITHIN ONE YEAR**

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
Trade debtors	124	87	-	-
Amounts owed by group undertakings	-	-	46	44
Other debtors	3	2	-	-
Corporation tax	24	13	-	-
Prepayments and accrued income	10	12	-	-
	<u>161</u>	<u>114</u>	<u>46</u>	<u>44</u>

Amounts owed by group undertakings to the Company include an intercompany loan due to SGN Midco Limited from SGN Natural Gas Limited amounting to £41m (2022: £40m). The loan bears interest at the Bank of England Base Rate plus 1% per annum and it is repayable on demand.

Also included are intercompany trade balances due from the SGN Group to the Company of £5m (2022: £4m).

17. SHORT TERM DEPOSITS

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
Short term deposits	<u>210</u>	<u>55</u>	<u>4</u>	<u>9</u>

18. CASH AT BANK

	Group	
	2023	2022
	£m	£m
Cash at bank	<u>43</u>	<u>25</u>

Cash and cash equivalents contain £41m (2022: £25m) of cash which is contractually restricted to be used on designated innovation projects only and is not available for general use.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****19. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR**

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
£165m 2.127% RPI-linked note due 2022*	-	266	-	-
£300m 4.875% fixed rate note due 2023*	300	-	-	-
Floating rate debt: bank facility	-	30	-	-
Trade creditors	77	49	-	-
Amounts owed to group undertakings	9	6	-	-
Social security and other taxes	22	20	-	-
Other creditors	15	13	-	1
Accrued interest	46	41	-	-
Deferred income	54	52	-	-
Accruals	135	106	-	-
	<u>658</u>	<u>583</u>	<u>-</u>	<u>1</u>

* Listed on the London Stock Exchange

Included in floating rate debt falling due within one year for the comparative period is a revolving credit facility of £30m. The total revolving credit facility is £360m (2022: £360m) and expires in March 2025. This facility was undrawn as at 31 March 2023 (2022: £30m drawn).

Included in amounts owed by group undertakings are intercompany trade balances due to fellow subsidiaries of Scotia Gas Networks Limited of £9m (2022: £6m).

In the year ended 31 March 2021, Scotland Gas Networks plc entered into an agreement with Ofgem to deliver a hydrogen gas pilot project in Scotland, known as the H100 Fife Project. In FY21 and FY22, the Group received £26m of upfront funding from the Scottish government, Ofgem and other Gas Distribution Networks, which was recorded as Cash at bank and Trade creditors on the Consolidated balance sheet. Scotland Gas Networks plc subsequently entered into an intra-group arrangement with a fellow subsidiary of Scotia Gas Networks Limited, SGN Futures (H100) Limited, which is constructing the project on behalf of the entity. Scotland Gas Networks plc releases the funding to SGN Futures (H100) Limited in line with contractual terms, which is capped at £25m. As at 31 March 2023 the Group holds £13m within Trade creditors and £25m within Cash at bank on the Consolidated balance sheet in relation to the H100 project.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****20. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR**

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
Bank loans (see note 21)	4,740	4,528	459	440
Derivative financial instruments				
Interest rate swaps	28	57	-	-
Inflation-linked swaps	73	74	-	-
Cross-currency swaps	15	-	-	-
	<u>4,856</u>	<u>4,659</u>	<u>459</u>	<u>440</u>

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

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
Fixed rate debt:				
£300m 4.875% fixed rate due 2023*	-	300	-	-
£350m 2.500% fixed rate due 2025*	349	348	-	-
£35m 2.407% fixed rate due 2025	35	35	-	-
£250m 3.25% fixed rate due 2027*	248	248	-	-
£375m 4.875% fixed rate due 2029*	374	374	-	-
£100m 2.90% fixed rate note due 2030	99	99	99	99
£150m fixed rate USPP due 2030	150	150	-	-
£250m 1.250% fixed rate note due 2031*	248	248	-	-
£75m 1.980% fixed rate due 2032	75	75	-	-
£34m 6.220% fixed rate note due 2032	34	-	-	-
£50m 2.040% fixed rate due 2033	50	50	-	-
£185m 3.02% fixed rate note due 2033	183	182	183	182
£150m fixed rate USPP due 2033	150	150	-	-
\$66m 5.630% fixed rate note due 2033	53	-	-	-
£100m 2.270% fixed rate due 2034	100	100	-	-
£225m 4.875% fixed rate due 2034*	225	225	-	-
£30m 6.310% fixed rate note due 2035	30	-	-	-
£50m 6.220% fixed rate note due 2035	50	-	-	-
\$66m 5.730% fixed rate note due 2035	53	-	-	-
£400m 3.1% fixed rate note due 2036*	398	398	-	-
£70m 6.340% fixed rate note due 2037	70	-	-	-
£15m 3.11% fixed rate note due 2038	15	15	15	15
£225m 6.38% fixed rate due 2040*	224	224	-	-
	<u>3,213</u>	<u>3,221</u>	<u>297</u>	<u>296</u>

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**20. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR - continued****Inflation-linked debt:**

£150m 2.066% RPI-linked due 2025*	273	242	-	-
£15m 2.580% RPI-linked loan due 2028	25	22	-	-
£50m -0.8818% CPI-linked loan due 2029	55	-	-	-
£50m -0.4465% CPI-linked loan due 2032	55	-	-	-
£38m RPI-linked due 2033	49	43	49	43
£250m 2.013% RPI-linked due 2035*	303	269	-	-
£88m RPI-linked due 2038	113	101	113	101
£125m 2.31% RPI-linked due 2039*	209	185	-	-
	<u>1,082</u>	<u>862</u>	<u>162</u>	<u>144</u>

Floating rate debt:

£125m floating rate note due 2025	125	125	-	-
£80m floating rate note due 2026	80	80	-	-
£90m floating rate note due 2026	90	90	-	-
£70m floating rate note due 2026	70	70	-	-
£80m floating rate loan note due 2043*	80	80	-	-
	<u>445</u>	<u>445</u>	<u>-</u>	<u>-</u>

Total debt	<u><u>4,740</u></u>	<u><u>4,528</u></u>	<u><u>459</u></u>	<u><u>440</u></u>
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* These bonds are listed on the London Stock Exchange.

Scotland Gas Networks plc and Southern Gas Networks plc debt instruments are unsecured, while MidCo's debt instruments are secured, and all are stated after the deduction of unamortised issue costs of £15m (2022: £16m). These costs together with the interest expense are allocated to the profit and loss account over the term of the debt. Interest is calculated using the effective interest rate method.

Certain interest costs in respect of RPI- and CPI-linked debt are not payable until the principal amount of the loans are repaid and are included within the carrying value of the debt stated above. Certain interest costs in respect of CPI-linked swaps are also not payable until the maturity of the swap. The amount of interest in relation to the RPI- and CPI-linked debt included in the carrying value of the debt at 31 March 2023 is £393m (2022: £384m) and £10m (2022: £nil) respectively. The amount of interest in relation to the CPI-linked swaps included in the carrying value of the debt at 31 March 2023 is £106m (2022: £36m).

In March 2022, Scotland Gas Networks Plc agreed to settle outstanding fees due in relation to certain guarantees provided by Ambac Assurance UK Limited that were previously in place over certain of the Company's outstanding public bond instruments, but which were removed in November 2020. The cash settlement amount of £4m is included within the "interest paid" line of the consolidated cash flow statement for the comparative period.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

20. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR - continued

Cash flow hedges

Included within creditors falling due after more than one year are cash flow hedges of £42m (2022:£57m). Cash flow hedges comprise a floating to fixed interest rate swap at Scotland Gas Networks plc, hedging future floating rate interest payments on a floating rate bond, and cross-currency swaps put in place at Southern Gas Networks plc to fully hedge the principal and interest payments on certain USD denominated private placement notes. For further details, see Note 21.

21. LOANS

An analysis of the maturity of bonds and bank loans is given below:

	Group		Company	
	2023	2022	2023	2022
	£m	£m	£m	£m
Between two and five years	1,423	1,673	-	-
After five years	3,317	2,855	459	441
	4,740	4,528	459	441
On demand or within one year	300	296	-	-
	5,040	4,824	459	441

22. FINANCIAL INSTRUMENTS

In the normal course of business, the Group is exposed to financial risks including, but not limited to, market, credit and liquidity risk. This note explains the Group's exposure to these risks, how they are measured and assessed, and summarises the policies and processes used to manage them.

The Group operates a centralised treasury function which is responsible for the management of financial risks of the Group as a whole and each of the regulated entities on a standalone basis. Financial risks comprise exposure to funding risk, liquidity risk, counterparty credit risk, interest rate risk, inflation risk, credit spread risk and foreign exchange risk. The treasury function does not operate as a profit centre, nor does it enter into speculative transactions.

The Group's treasury activities are overseen by the Finance Committee, which meets on a periodic basis throughout the financial year. The Finance Committee is comprised of four directors (one from each of the SGN Group's shareholders) plus one statutory independent non-executive director. The Group's Treasurer reports on a regular basis to the Finance Committee.

The Board reviews and approves all major treasury decisions.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS – continued

Liquidity risk

Liquidity risk represents the risk of having insufficient funds to meet its financing in any particular subsidiary when needed.

To manage this risk the Group has a policy of actively maintaining a mixture of medium-term and long-term debt alongside committed facilities and short-term cash investments to ensure that the Group has sufficient available funds to meet forecast requirements over the short-term to medium-term. As part of their regulatory license Scotland Gas Networks plc and Southern Gas Networks plc are required to submit an annual certificate to their regulator, which includes a confirmation of sufficiency of financial resources (liquidity looking forward 12 months). The same principles are also applied across the wider Group.

To prevent over-reliance on individual sources of liquidity, funding is accessed across a range of instruments including public bonds, bank loan facilities (including the RCF), private placements and EIB loans.

The Group currently has external financing (including undrawn revolving credit facilities) outstanding across three of the Group's subsidiaries:

- SGN MidCo Limited: £162m inflation-linked private placements and £297m fixed rate private placements;
- Scotland Gas Networks plc: £474m fixed rate bonds; £80m floating rate bonds; £210m inflation-linked bonds; £458m fixed rate private placements; £100m EIB loans; £20m (undrawn) bank RCF; and £110m inflation-linked bank term loan facility; and
- Southern Gas Networks plc: £1,894m fixed rate bonds; £601m inflation-linked bonds; £356m fixed rate private placements; and £300m EIB loans; and £340m (undrawn) bank RCF.

Group subsidiaries are also funded through a combination of share capital, retained earnings and intercompany loans.

Cash pooling structures are used to centralise surplus cash balances held by subsidiaries where possible to minimise external borrowings and interest costs. The treasury function seeks to minimise cash balances by conducting a detailed cash flow forecast process and timing funding issuance appropriately, however where surplus cash balances do arise, these are invested in highly rated bank deposits and money market funds.

The contractual maturity of the Group's financial assets and liabilities are shown in the following tables. The amounts shown are gross cash inflows/(outflows), including interest, with the exception of financial derivatives settled on a net basis where the amounts represent undiscounted net cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to relevant conditions existing at the reporting date.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

2023

	0-6 months £m	6-12 months £m	1-2years £m	2-5years £m	>5years £m	Contractual cashflows £m	Interest / discounting £m	Carrying value £m
Financial liabilities								
loans and borrowings								
Bank facility	-	-	-	-	-	-	-	-
Bonds	(64)	(402)	(537)	(1,442)	(4,372)	(6,816)	1,777	(5,040)
	(64)	(402)	(537)	(1,442)	(4,372)	(6,816)	1,777	(5,040)
Derivative financial liabilities								
Inflation - linked swaps	(10)	(12)	(22)	(69)	302	189	(262)	(73)
Interest rate swaps	1	1	2	6	34	44	(72)	(28)
Cross-currency swaps	1	4	7	22	163	197	(212)	(15)
	(8)	(7)	(13)	(41)	499	430	(546)	(116)
Other financial liabilities								
Trade and other creditors	(77)	-	-	-	-	(77)	-	(77)
	(149)	(409)	(550)	(1,483)	(3,873)	(6,463)	1,231	(5,233)

The Group expects to meet its obligations from cash balances, operating cash flows and refinancing. The maturity date of the bank facility is January 2024 but is classified as short-term as the facility requires extending at the end of each applicable interest period.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****22. FINANCIAL INSTRUMENTS - continued**

The corresponding amounts for 2022 were as follows:

2022

	0-6 months £m	6-12 months £m	1-2years £m	2-5years £m	>5years £m	Contractual cashflows £m	Interest / discounting £m	Carrying value £m
Financial liabilities								
loans and borrowings								
Bank facility	(30)	-	-	-	-	(30)	-	(30)
Bonds	(80)	(367)	(434)	(1,369)	(4,368)	(6,618)	1,824	(4,794)
	(110)	(367)	(434)	(1,369)	(4,368)	(6,648)	1,824	(4,824)
Derivative financial liabilities								
Inflation - linked swaps	(10)	(12)	(22)	(67)	251	140	(214)	(74)
Interest rate swaps	2	2	4	13	69	90	(147)	(57)
	(8)	(10)	(18)	(54)	320	230	(361)	(131)
Other financial liabilities								
Trade and other creditors	(49)	-	-	-	-	(49)	-	(49)
	(167)	(377)	(452)	(1,423)	(4,048)	(6,467)	(1,463)	(5,004)

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

Credit risk

Credit risk represents the risk that a counterparty does not settle an obligation for full value when that amount becomes due.

The Group is primarily exposed to credit risk arising from the extension of credit to its customers, cash deposits, derivatives and amounts due from external financing counterparties arising on certain committed facilities and financial instruments.

The maximum exposure to credit risk is the carrying value of financial assets as follows:

	2023	2022
	£m	£m
Net trade receivables	124	87
Other debtors	3	2
Short term deposits	210	55
Cash	43	25
	<u>380</u>	<u>169</u>

Trade and other receivables:

Our principal debtor exposure is governed by the credit rules within the Uniform Network Code. This sets out the level of credit relative to the RAV for each credit rating. Our credit policies and practices are designed to limit credit exposure by collecting security deposits prior to providing utility services, or after utility service has commenced if certain applicable regulatory requirements are met. Collection activities are managed daily. The utilisation of credit limits is regularly monitored and collateral is collected against these accounts when necessary.

Trade debtors predominantly relate to transportation income from gas shippers. Credit risk arising from the Group's regulated business is managed in accordance with industry standards as set out by the Unified Network Code. The Group contracts with shippers having investment grade ratings only, or where suitable collateral or cash prepayments are made. The Group currently holds £31m of security in respect of its trade counterparties (2022: £18m). These are included in trade creditors as at the year end.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**22. FINANCIAL INSTRUMENTS - continued**

The largest transportation debtor is £19m (2022: £20m). There is no material credit exposure to any one customer. The ageing of trade debtors net of impairment allowance is:

	2023	2022
	£m	£m
Not past due	118	81
Past due 0-30 days	-	-
Past due 31-90 days	-	1
Past due over 90 days	6	5
	<u>124</u>	<u>87</u>

The maximum exposure to credit risk at the reporting date is the fair value of each class of debtors mentioned above.

At the end of each reporting year a review of the provision for bad and doubtful debts is performed taking into account the age, status and risk of recovery for each debtor.

Financial instruments:

The Group seeks to minimise its exposure to counterparties under financial instruments by agreeing individual exposure limits with the Finance Committee for financial instruments (based on instrument types and counterparty credit ratings) and by diversifying exposure across a range of counterparties. Counterparty credit ratings are monitored by the treasury function on a regular basis and ISDA agreements are in place with all counterparties to permit net settlement of assets and liabilities across certain financial instruments.

Counterparty credit risk arising from financial derivatives are managed through the maintenance of financial limits according to defined criteria, subject to a minimum credit rating of A-/A3 for new transactions and at credit ratings below this level counterparties are required to cash post collateral for mark to market positions owed to the regulated businesses within the Group. Investments of cash through deposits in the short-term are also subject to review and approval according to defined criteria agreed by the Finance Committee and Board.

The Group conducted a review of counterparty credit risk and its own credit risk and concluded that an adjustment was required to reflect the net credit risk in arriving at the fair value of financial instruments stated in the balance sheet. The net credit risk adjustment reduced liabilities by £36m (2022: £32m), of which £29m (2022: £32m) related to inflation-linked swaps, £4m (2022: £nil) to interest rate swaps and £3m (2022: £nil) to cross-currency swaps. £29m (2022: £32m) was credited to the consolidated profit and loss account in the line 'Fair value movements on derivatives' and £7m (2022: £nil) was credited to other comprehensive income. The net credit risk adjustment was debited to 'Derivative financial liabilities' within 'Creditors: amounts falling due after more than one year' as presented in the consolidated balance sheet.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

The net credit risk adjustment represents the risk of non-performance (or default) of either the counterparty or the Group in relation to financial instruments that require fair value measurements. These adjustments are respectively called Credit Value Adjustments ('CVA') and Debit Value Adjustments ('DVA').

The CVA and DVA are calculated by running two separate Monte Carlo simulations, based on the bilateral credit risk adjustment method. Quoted credit default swap spreads ('CDS') are used to determine counterparty credit curves when calculating the CVA. Z-spreads of senior unsecured public bonds are used to construct a credit curve for the Group when calculating the DVA.

The net credit risk adjustment is made up of a CVA of £3m (2022: £2m) and a DVA of £(40)m (2022: £(34)m). The magnitude of the DVA adjustment as at 31 March 2023 is mainly due to the asymmetric cash flow positions. SGN settle the inflation accretion to the counterparty at maturity on the swap, whereas the Group receive cash flows from the counterparty at every interest rate settlement date (every six months) through to maturity. The inflation linked swaps are long dated with remaining tenors of between 9-14 years, exacerbating the impact of the asymmetric cash flow position.

The Mark to Market ('MtM') value is calculated using a discounted cash flow method, which discounts the contracted future cashflows of derivatives using a risk-free rate (SONIA). The valuation is subsequently adjusted for the default risk of both the bank counterparty and the SGN entity respectively, by applying the CVA and DVA (together the 'net credit risk adjustment').

Market risk

Market risk represents the risk of losses or other adverse effects resulting from adverse changes in market prices or from unfavourable market conditions.

The Group is primarily exposed to market risk on UK interest rate; UK inflation rates and credit spreads in general.

Interest rate risk:

The Group's interest rate risk arises as a result of two primary sources:

- The mechanisms that the regulators have implemented to determine revenues for the Group's regulated businesses; and
- New and existing borrowings and financial instruments net of cash and cash equivalents, with the primary exposures arising from fluctuations in Sterling interest rates.

Certain of the Group's financing arrangements carry requirements to maintain exposure to fixed interest rates or inflation-linked above a certain level/within a range.

The Group manages its exposure to interest rate risk by targeting issuance in the most efficient markets available to achieve desired size and duration and using derivative financial instruments to manage the ultimate exposure to fixed/floating interest rates, if required. In addition, the Group aims to maintain a smooth maturity profile across all debt instruments to ensure that there is no significant concentration of interest rate exposure when refinancing maturing debt.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

The following table represents the annualised impact (net of deferred tax) of 100 basis point change in short-term interest rates at the reporting date in relation to equity and profit and loss account. The analysis assumes that all other variables remain constant.

	2023 £m	2022 £m
Impact on profit and loss account		
Floating rate instruments	(5)	(4)
Fixed to floating swaps	(1)	-
Floating to fixed swaps	-	-
	<u>-</u>	<u>-</u>
Total	<u>(6)</u>	<u>(4)</u>
Impact on equity		
Floating to fixed swaps	1	1
	<u>1</u>	<u>1</u>

Inflation risk:

The Group's inflation risk arises as a result of three primary sources:

- The mechanisms that the regulators have implemented to determine revenues for the Group's regulated businesses;
- Impact on controllable and non-controllable costs; and
- New and existing borrowings and financial instruments net of cash and cash equivalents, with the primary exposures arising from fluctuations in UK CPIH, CPI and RPI.

Certain of the group's financing arrangements carry requirements to maintain exposure to fixed interest rates or inflation-linked above a certain level/within a range.

The Group manages its exposure to inflation rate risk by targeting issuance in the most efficient markets available to achieve desired size and duration and using derivative financial instruments to manage the ultimate exposure to inflation if required.

Certain of the Group's inflation-linked borrowings and financial instruments, including interest liabilities are exposed to a risk of changes in the carrying value due to changes in the UK Retail Price Index ('RPI') and UK Consumer Price Index ('CPI'). The movements in these forms of liability offer a correlation to the movements in the Group's regulatory asset value which in the RIIO-GD2 price control is linked to CPIH due to the pricing mechanism imposed by the Regulator. The turnover capacity charges are also linked to CPIH. There is currently limited capacity in capital and financial markets to provide borrowings or financial instruments that are linked to CPIH.

By matching liabilities and assets in this way, inflation-linked borrowings and financial instruments partially hedge the exposure to changes in inflation.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued**
for the Year Ended 31 March 2023**22. FINANCIAL INSTRUMENTS - continued**

The following table shows the illustrative effect on the profit and loss account that would result from a 1% movement in RPI and CPI before the effects of tax.

	2023 £m	2022 £m
Impact on profit and loss		
Inflation-linked bonds	11	17
Inflation-linked swaps	8	-
Transportation income	(12)	(10)
Total	7	7

Credit spread risk:

The Group's credit spread risk arises as a result of the capital structure that is maintained, currently with external committed debt and facilities totalling £5,547m (2022: £5,307m) (including undrawn bank facilities but excluding shareholder loans and gross unamortised issue costs). Lenders and investors assess the credit quality of the borrowing entity and charge a spread above benchmark rates to determine the overall return they require (and as a result the interest rate that the borrowing entity pays). Credit spreads can be impacted by both the specific credit risk of the borrower and macro events as well as general investor appetite for debt investments.

The Group manages its exposure to credit spreads by maintaining access to a diversified range of debt markets so that there is less exposure to a single group of investors/lender. The Group also maintains credit ratings with Fitch; Moody's and Standard & Poor's (S&P), with regular meetings and dialogue to support their appraisal, which ensures that a clear independent indication of the Group's credit risk is available to investors. In addition, the Group aims to maintain a smooth maturity profile across all debt instruments to ensure that there is no significant concentration of credit spread exposure when refinancing maturing debt.

Foreign exchange risk - transaction:

The Group is exposed to movements in foreign exchange rates due to its commercial trading transactions, however the volume of foreign denominated payments and receivables is not considered material and no active hedging of foreign exchange transactions is undertaken.

Foreign exchange risk - translation:

The Group seeks to match the currency of borrowings to the currency of its underlying investments. As the Group's assets are materially denominated in Sterling, the Group and its subsidiaries seek to source Sterling debt. Debt is sourced from the most appropriate market or markets available at the time of raising new finance (including foreign currency markets) and appropriate derivative financial instruments transacted to manage the proceeds into the appropriate currency. In the current financial year, the Group issued USD denominated private placement notes that it fully hedged back to Sterling at issuance using cross-currency swaps. The Group has also issued private placement notes in the US that are denominated in Sterling where the underlying exposure is USD. On these transactions the noteholder has transacted a derivative financial instrument to hedge the USD exposure into Sterling and as a result the Group does not have exposure to USD under the transactions.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

Cash flow hedges

Cash flow hedges comprise a floating to fixed interest rate swap at Scotland Gas Networks plc, hedging future floating rate interest payments on a floating rate bond, and cross-currency swaps put in place at Southern Gas Networks plc to fully hedge the principal and interest payments on certain USD denominated private placement notes. Receipts and payments for the swaps and the underlying bonds are exactly matched and in accordance with IAS 39 any gain or loss that is deferred to equity is recognised in profit or loss over the period that the floating rate interest payments impact on profit.

The interest rate swap at Scotland is in place to hedge future interest outflows on the floating rate bond and is therefore an effective hedging instrument.

The movement before deferred tax taken to the hedging reserve in equity in respect of this cash flow hedge in the year was a £26.9m gain (2022: £15.5m gain) and the ineffective portion of this hedge of £2.1m was credited to the profit and loss account (2022: £nil). The hedge reserve movement is expected to unwind in profit or loss over the life of the swaps.

The notional principal amount of the outstanding cashflow hedges at 31 March 2023 was £80.0m (2022: £80.0m). As at 31 March 2023, the fixed rate of interest on this swap was 7.0575% and the floating rate was SONIA + 1.1193%. The uncompounded SONIA rate as at 31 March 2023 was 4.1777%.

Cross-currency swaps

The movement before deferred tax taken to equity in respect of cross-currency swaps in the year was a £15m loss (2022: £nil) of which £9m was recycled to the profit and loss account to neutralise the effect of foreign exchange on the underlying bonds. The notional principal amount of the pay leg of the outstanding cross-currency swaps at 31 March 2023 amounted to £116m (2022: £nil), whilst the receive leg totalled \$132m. As at 31 March 2023, the fixed rates of interest paid on these swaps were 6.2435%; 6.2585 and 6.2800%. The fixed rates of interest received were 5.63% and 5.73%.

Categories of financial instruments

The categories of financial assets and liabilities held by the Group were as follows:

	Book value	
	2023	2022
	£m	£m
Financial assets held at amortised cost		
Trade debtors [1]	124	87
Short term deposits [1]	210	55
Other debtors	3	2
Cash	43	25
	380	169

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****22. FINANCIAL INSTRUMENTS - continued****Financial assets held at fair value**

Derivative financial instruments:

- Interest rate swaps

5	-
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5	-
---	---

Total financial assets

385	169
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[1] The carrying amount of financial assets approximate to their fair value

	Book value	
	2023	2022
	£m	£m
Financial liabilities held at amortised cost		
Trade creditors	77	49
Accrued interest	46	41
Accruals	135	106
Fixed rate debt	300	-
Floating rate debt	-	30
Inflation-linked debt	-	266
Borrowings	4,740	4,528
	5,298	5,020
Financial liabilities at fair value		
Derivative financial instruments:		
- Inflation-linked swaps	73	74
- Interest rate swaps	28	57
- Cross-currency swaps	15	-
	116	131
Total financial liabilities	5,414	5,151

The carrying amount of financial liabilities approximates to their fair value except for bonds, the fair value of which is disclosed below.

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

- Level 1: Valued using unadjusted quoted prices in active markets for identified financial instruments;
- Level 2: Valued using techniques based significantly on observable market data. Instruments in this category are valued using valuation techniques where all of the inputs that have a significant impact on the valuation are directly or indirectly based on observable market data;
- Level 3: Instruments in this category have been valued using a valuation technique where at least one input (which has a significant input on the financial instruments' valuation) is not based on observable market data. Where inputs can be observed from market data with not undue cost and effort, the observed input is used. Otherwise, management determines a reasonable estimate for the input.

An analysis of financial assets and liabilities that are recorded at fair value at 31 March 2023 is as follows:

	2023			Total
	Level 1 £m	Level 2 £m	Level 3 £m	£m
Financial assets				
At fair value through profit and loss				
Derivative financial instruments:				
- Interest rate swaps	-	5	-	5

Financial liabilities				
At fair value through profit and loss				
Derivative financial instruments:				
- Inflation-linked swaps	-	73	-	73
- Interest rate swaps	-	28	-	28
- Cross-currency swaps	-	15	-	15
	-	116	-	116

	2022			Total
	Level 1 £m	Level 2 £m	Level 3 £m	£m
Financial liabilities				
At fair value through profit and loss				
Derivative financial instruments:				
- Mirror swaps	-	74	-	74
- Interest rate swaps	-	57	-	57
	-	131	-	131

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

Inflation-linked swaps

In the comparative period, during the 12 months to 31 March 2022, Southern Gas Networks plc and Scotland Gas Networks plc transacted £540m and £130m of CPI-linked swaps respectively, which economically convert some or all of the notional principal of the following existing fixed rate debt instruments into CPI-linked debt instruments:

- £75m fixed rate notes maturing for Southern Gas Networks plc in 2030;
- £75m fixed rate notes maturing for Scotland Gas Networks plc in 2030;
- £250m fixed rate bond maturing for Southern Gas Networks plc in 2031;
- £75m fixed rate notes maturing for Southern Gas Networks plc in 2033;
- £55m fixed rate notes maturing for Scotland Gas Networks plc in 2033;
- £100m fixed rate notes maturing for Southern Gas Networks plc in 2034; and
- £40m of the £400m fixed rate bonds maturing for Southern Gas Networks plc in 2036.

Mirror swaps

In 2005 the Group entered into interest rate swap contracts to fix the Group's interest cost relating to floating rate bridging loans, which were later replaced by permanent long-term capital markets debt. At that point the interest rate swaps became obsolete and consequently matching swaps were transacted (under which the Group received fixed rate interest) to close out the position. In March 2022 both sides of the mirror swaps were terminated with the mark to market value cash settled for a total consideration of £21m. The debit has been taken to the financial instruments liability in the balance sheet and a difference of £0.9m between the carrying mark to market value of the swaps compared and the settlement value has been written off within the interest receivable and similar income line in the profit and loss account. This resulted in the elimination of any liability for the mirror swaps on the Group's balance sheet. The £21m cash settlement was recognised in the "payments of mirror swaps" line of the cash flow statement, within cash flows from financing activities.

Interest rate swaps

In October 2022, Scotland Gas Networks plc entered into three interest rate swaps totalling £90m that convert some or all of the £184m fixed rate notes, entered into within the same month, into floating rates based on SONIA:

- £30m of the £34m notes due 2032 converted from fixed to SONIA plus 2.115%, effective October 2022;
- £30m of the £30m notes due 2035 converted from fixed to SONIA plus 2.373%, effective March 2023;
- £30m of the £50m notes due 2035 converted from fixed to SONIA plus 2.2695%, effective October 2022.

In June 2022 the mandatory break on Scotland Gas Networks plc's £80m IRS was extended by 10 years to March 2033. As part of this exercise, the swap was novated to another of the Group's relationship banks and the fixed rate payable leg was increased by around 0.5%. The floating rate receivable was unchanged and remains the same as the floating rate payable on the hedged £80m floating rate bond due 2043.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

22. FINANCIAL INSTRUMENTS - continued

In February 2023, Scotland Gas Networks plc entered into a single £30m interest rate swap to 're-fix' the interest rate swap hedging the fixed rate notes due in 2032. The new swap's floating receive leg exactly offsets the original swap's floating pay leg, resulting in a net fixed exposure.

Cross-currency swaps

In October 2022, Southern Gas Networks plc issued a total of \$132m in private placement notes, for which drawing occurred in March 2023:

- \$66m 5.63% fixed rate notes due 2033;
- \$66m 5.73% fixed rate notes due 2035.

In line with the Company's hedging policy, the entire principal amounts and interest payments under these notes have been hedged using cross currency-swaps with effective dates matching the drawdown profiles of the notes. Under these cross-currency swaps, the Company receives a USD upfront payment and fixed USD payments equal to the principal amounts and coupons under the notes respectively, and pays fixed GBP amounts:

- \$41m converted to £36m with fixed 6.2440% GBP interest payable, due 2033, effective March 2023;
- \$25m converted to £22m with fixed 6.2485% GBP interest payable, due 2033, effective March 2023;
- \$66m converted to £59m with fixed 6.2800% GBP interest payable, due 2035, effective March 2023.

Fair values

The Group's financial instruments recorded at amortised cost are shown below together with their fair values:

	31 March 2023		31 March 2022	
	Book value	Fair value	Book value	Fair value
	£m	£m	£m	£m
Borrowings	5,040	5,240	4,794	5,703
Bank facility	-	-	30	30
	<u>5,040</u>	<u>5,240</u>	<u>4,824</u>	<u>5,733</u>

Fair values of borrowings have been determined by reference to closing quoted market values where available or otherwise by discounting future cash flows at their market interest rate.

The carrying value of all other financial assets and liabilities approximates to their book value.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****23. PROVISIONS FOR LIABILITIES**

	Group	
	2023	2022
	£m	£m
Deferred tax	<u>1,060</u>	<u>1,062</u>
Other provisions		
Other provisions	29	16
Environmental provisions	<u>13</u>	<u>14</u>
	<u>42</u>	<u>30</u>
Aggregate amounts	1,102	1,092

Group

	Deferred tax	Other provisions
	£m	£m
Balance at 1 April	1,062	30
Utilised during year	-	(2)
Discount unwind	-	1
Net movement in deferred tax	(2)	-
Reassessments during the year	<u>-</u>	<u>13</u>
Deferred tax	<u>1,060</u>	<u>42</u>

The discount unwind on environmental provisions, included in interest payable and similar expenses in the profit and loss account, was £435,354 (2022: £262,146).

Environmental

The environmental provision represents the Directors' best estimate of environmental restoration costs, where the Group has a legal obligation to restore sites at the balance sheet date. The provision has been discounted at the nominal rate of 3.21% (2022: 1.45%) and is stated at the present value of the estimated expenditure to settle the obligation. The provision is expected to be utilised over the next three years in line with anticipated regulatory outputs requirements for land remediation.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**23. PROVISIONS FOR LIABILITIES - continued****Deferred tax**

Deferred tax is provided as follows:

	Group	
	2023	2022
	£m	£m
Accelerated capital allowances	(1,000)	(995)
Deferred tax on inflation swaps	(6)	10
Deferred tax on cash flow hedges	7	14
Deferred tax on defined pension benefits	(61)	(91)
	<hr/>	<hr/>
Deferred tax	(1,060)	(1,062)

The movement in provision for deferred tax is as follows:

	Group	
	2023	2022
	£m	£m
Opening balance	(1,062)	(813)
Charged to profit and loss account	(22)	(230)
Credited/(charged) to other comprehensive income	24	(19)
	<hr/>	<hr/>
Deferred tax	(1,060)	(1,062)

The Company has no deferred tax assets or liabilities (2022: nil).

The Group is not expecting a reversal of deferred tax in the next financial year.

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

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

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

The Company has no unrecognised deferred tax assets or liabilities.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued**
for the Year Ended 31 March 2023**23. PROVISIONS FOR LIABILITIES - continued****Other provisions**

Other provisions consist of asbestos related liabilities and other provisions relating to the operations of our gas networks, including the Operational target provision, detailed in Note 2. The other provisions represent management's best estimates of the future expenditure necessary to settle the obligations. The provision has been discounted and is stated at the present value of the estimated expenditure to settle the obligation. The asbestos related provision is expected to be utilised over the next 29 years. The other provisions relating to the operations of our gas networks are expected to be utilised in the next 2 years.

24. DEFERRED INCOME

	Group	
	2023	2022
	£m	£m
Deferred income	<u>483</u>	<u>461</u>

Customer contributions

The Group has received customer contributions relating to plant and machinery. In accordance with the Group's accounting policy the assets are capitalised within fixed assets and the contributions are recognised as deferred income in the balance sheet. The connections contributions are from customers being connected to the network and replacement contributions are related to the diversion of gas mains.

The deferred income is released to the profit and loss account over the estimated lives of the related assets.

The amount deferred under this policy was as follows:

	Connections	Replacement	Total	Total
	2023	2023	2023	2022
	£m	£m	£m	£m
Customer contributions brought forward	273	188	461	434
Customer contributions deferred in year	19	14	33	37
Amortisation in year	<u>(7)</u>	<u>(4)</u>	<u>(11)</u>	<u>(10)</u>
	<u>285</u>	<u>198</u>	<u>483</u>	<u>461</u>

The Company has no deferred income in the current year or the previous year.

Customer contributions exclude Deferred income presented as part of Creditors: Amounts falling due within one year, as those amounts relate to unfinished projects, where the associated asset is not yet completed.

SGN Midco Limited (Registered number: 11050000)**Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023****25. CALLED UP SHARE CAPITAL**

Allotted, issued and fully paid:

Number:	Class:	Nominal value:	2023 £m	2022 £m
2,815,000,001	Ordinary	£0.01	<u>28</u>	<u>28</u>

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

**26. RESERVES
Group**

	Profit and loss account £m	Hedging reserves £m	Merger reserve £m	Totals £m
At 1 April 2022	3,931	(41)	(2,787)	1,103
Profit for the year	143	-	-	143
Dividends	(70)	-	-	(70)
Movement in cash flow hedges	-	16	-	16
Remeasurement of net defined benefit asset	<u>(88)</u>	<u>-</u>	<u>-</u>	<u>(88)</u>
At 31 March 2023	<u>3,916</u>	<u>(25)</u>	<u>(2,787)</u>	<u>1,104</u>

Company

	Profit and loss account £m
At 1 April 2022	2,399
Profit for the year	49
Dividends	<u>(70)</u>
At 31 March 2023	<u>2,378</u>

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

The merger reserve shows difference between the consideration paid and the book value of the net assets acquired at the time of the Group restructure in December 2017.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

27. EMPLOYEE BENEFITS

A proportion of the Group's employees are members of the Scotia Gas Networks Pension Scheme ('the Scheme'). The Scheme provides final salary defined benefits for employees who joined the Lattice Group Scheme prior to 31 March 2002. Under the Scheme, the employees are entitled to retirement benefits based on final salary on attainment of retirement age (or earlier withdrawal or death). The Scheme is open to future accrual of benefits and closed to new members. Employees joining the Lattice Company Scheme after 31 March 2002 were entitled to join a defined contribution scheme.

Defined contribution schemes

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

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

	2023	2022
	£m	£m
Amount charged in respect of defined contribution schemes	<u>15</u>	<u>13</u>

Defined benefit schemes

The Scheme is operated by the Scotia Gas Networks Limited and is funded with assets held in separate trustee administered funds. It is subject to independent valuations at least every three years, on the basis of which the qualified actuary determines the rate of employers' contribution, which, together with the specified contributions payable by the employees and proceeds from the scheme's assets, are expected to be sufficient to fund the benefits payable under the scheme. Under the Group cost allocation plan, the Group accounts for its agreed share of the total net defined benefit cost, based on the proportionate members relating to the Group.

The most recent triennial valuation of the Scheme was carried out at 31 March 2021. The Group has employed an independent actuary to approximately update this valuation allowing for differences between the actuarial assumptions used by the Scheme for funding purposes and those adopted by the Group to measure the Scheme's liabilities on the financial statements, as well as adjusting for benefit accrual and benefits paid by the Scheme. The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method. In accordance with FRS 102, a limited actuarial review has been carried out by Broadstone Corporate Benefits Limited at 31 March 2023 using the projected unit method.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**27. EMPLOYEE BENEFITS - continued**

The following financial assumptions have been used:

	As at 31 March 2023	As at 31 March 2022
Key assumptions used:		
Retail price inflation	3.5% p.a.	3.8% p.a.
Consumer price inflation	3.1% p.a.	3.4% p.a.
Rate of increase of pensions	3.5% p.a.	3.8% p.a.
Rate of increase of salaries	3.3% p.a.	3.6% p.a.
Discount rate	<u>4.7% p.a.</u>	<u>2.8% p.a.</u>

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

The assumptions relating to longevity underlying the pension liabilities reflect the characteristics of the Scheme membership ('VitaCurves') for base mortality with an allowance for further improvements in life expectancy in line with the medium cohort adjustments subject to a 1.5% p.a. underpin in the longevity assumption. The assumed life expectancy in years for a member once they reach age 65 is as follows:

As at 31 March	2023		2022		2021	
	Male	Female	Male	Female	Male	Female
Members currently aged 65	22.3	24.7	22.8	24.4	22.7	24.3
Members currently aged 45	24.3	26.8	24.5	27.0	24.4	26.9

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

	Sensitivity	Approximate change in DBO £000
Discount rate	+ 0.1% p.a.	(9,100)
	- 0.1% p.a.	9,300
Price inflation (RPI measure)*	+ 0.1% p.a.	8,500
	- 0.1% p.a.	(8,800)
Life expectancy	+ 1 year	25,700
	- 1 year	(24,600)

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

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**27. EMPLOYEE BENEFITS - continued**

The fair value of the assets in the scheme and the present value of the liabilities in the scheme were:

Fair value as at 31 March	2023			2022		
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equities	-	-	-	127	-	127
Government bonds [1]	404	-	404	535	-	535
Corporate bonds	136	103	239	190	110	300
Property	-	-	-	-	1	1
Cash	-	11	11	-	11	11
Insurance contracts	-	199	199	-	247	247
Total market value of assets	540	313	853	852	369	1,221
Actuarial value of liabilities			(607)			(858)
Net pension asset			246			363

[1] Including LDI repurchase agreement liabilities.

The fair value of scheme assets at 31 March 2023 are based on the bid price where available. The fair value of property is based on the mid-price and the value of the single unit price funds is based on the single unit price.

To reduce the risk of volatility in the Scheme's funding level, a liability driven investment (LDI) strategy forms part of the assets employed within the investment strategy of the Scheme. The LDI strategy contributes to overall hedging levels for the Scheme of 95% for interest rates and 95% for inflation as at 31 March 2023 with respect to the pension scheme liabilities of £0.6bn (valued using the UK government bond yield curve). These LDI assets, which provide both interest rate and inflation protection, are managed by BlackRock and include a variety of instruments, including UK Government bonds (gilts), interest rate swaps, inflation swaps, gilt repos and corporate bonds. Further interest rate protection is provided by investment grade credit funds, including those managed by BlackRock and Goldman Sachs. The Scheme has also implemented pensioner buy-ins which contribute to the total interest rate hedging ratios referred to above.

After considering the Scheme's strong funding level and the advice of the Scheme's investment advisors, in March 2023 the Scheme's trustees agreed to undertake some further de-risking of the investment portfolio and fully sell out of all equity positions. The proceeds of the sale were invested into LDI assets initially, with a longer-term investment strategy for the proceeds to be agreed by the Trustees over the course of the 2023/24 financial year.

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**27. EMPLOYEE BENEFITS - continued**

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

	2023	2022
	£m	£m
At 1 April	(859)	(937)
Current service cost	(16)	(18)
Interest cost	(22)	(19)
Actuarial gains	252	73
Benefits paid	38	43
	<u>38</u>	<u>43</u>
At 31 March	<u>(607)</u>	<u>(858)</u>

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

	2023	2022
	£m	£m
At 1 April	1,221	1,236
Interest income	32	25
Contributions from the Group	8	21
Remeasurement of scheme assets	(369)	(16)
Benefits paid	(38)	(43)
Administration costs	(1)	(2)
	<u>(1)</u>	<u>(2)</u>
At 31 March	<u>853</u>	<u>1,221</u>

The actual (loss)/ return on plan assets was:

	2023	2022
	£m	£m
Loss on plan assets excluding interest income	(369)	(16)
Interest income on plan assets	32	25
	<u>32</u>	<u>25</u>
Actual (loss)/return on plan assets	<u>(337)</u>	<u>9</u>

Employer contributions for the period ending 31 March 2022 were 37.3% (2022: 37.3%) of monthly salary roll, before allowing for any salary sacrifice contributions. Deficit contributions were not payable from 1 April 2022 (2022: £12.5m p.a. from 1 April 2021 to 31 March 2022).

The cumulative amount of actuarial gains recognised in the statement of comprehensive income since adoption is £273m (2022: £20m).

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**27. EMPLOYEE BENEFITS - continued**

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

	2023	2022
	£m	£m
Current service cost	(16)	(18)
Administration cost	(1)	(2)
Total charged to net operating costs:	(17)	(20)
Expected return on scheme assets	32	25
Interest charge on scheme liabilities	(22)	(19)
Net interest credit	10	6
Total charge to the profit and loss account	(7)	(14)

	2023	2022
	£m	£m
Actuarial loss on scheme assets	(369)	(16)
Actuarial gain on scheme liabilities	252	73
(Loss)/Gain recognised in other comprehensive income	(117)	57

SGN Midco Limited (Registered number: 11050000)Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**28. FINANCIAL COMMITMENTS****Capital commitments**

Capital projects contracted for by the Group but not provided in the financial statements amounted to £52m at 31 March 2023 (2022: £33m). The Company has no capital commitments at 31 March 2023.

Operating lease commitments

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

	Other		Land and Buildings	
	2023	2022	2023	2022
	£m	£m	£m	£m
- less than one year	2	2	2	1
- between two to five years	3	3	8	4
- after five years	-	-	21	14

Contingent liabilities

Through the ordinary course of operations, the Group is party to various litigation, claims and investigations.

In relation to the incident at Galpin's Road on 8 August 2022, the Group is continuing to support the police and Health and Safety Executive with their investigation. Due to the early stage of the investigation, it is not possible for management to reliably estimate the financial impact or timing of any future obligation as at 31 March 2023.

29. PARENT COMPANY AND RELATED PARTY TRANSACTIONS

The immediate parent undertaking is SGN PledgeCo Limited. The ultimate parent undertaking is Scotia Gas Networks Limited, a Company registered in England and Wales.

The largest group in which the results of the Company are consolidated is that headed by Scotia Gas Networks Limited, St Lawrence House, Station Approach, Horley, RH6 9HJ, United Kingdom.

Scotia Gas Networks Limited is owned by Apple Newco Limited (37.5%) which is indirectly wholly-owned by Ontario Teachers' Pension Plan Board, UK Gas Distribution 2 Limited (37.5%) which is indirectly wholly-owned by Brookfield Super-Core Infrastructure Partners and Speyside Bidco Limited (25.0%), which is wholly-owned by funds managed by Global Infrastructure Partners (GIP).

It is the opinion of the Directors that the parent Company, Scotia Gas Networks Limited, has no single controlling party.

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

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

29. PARENT COMPANY AND RELATED PARTY TRANSACTIONS - continued

Transactions with key management personnel

Total compensation of key management personnel in the year amounted to £6m (2022: £5m). Directors are also deemed to be key management personnel and their remuneration is disclosed in note 4.

Transactions with shareholders

During the year ended 31 March 2022, Scotia Gas Networks Limited underwent an ownership change and as such SSE plc ceased to be a shareholder and related party. In the year ended 31 March 2022, there were sales of goods and services amounting to £10m and purchase of goods and services of £(43m) between the Company and the SSE plc group of companies. Sales of goods and services to SSE primarily represented gas transportation services. At 31 March 2022 £nil was owed by SSE in relation to these services.

The Group had no transactions with shareholders or other related parties in the year ended 31 March 2023.

30. SUBSEQUENT EVENTS

In May 2023, Scotland Gas Networks plc entered into a single £30m interest rate swap to 're-fix' the interest rate swap hedging the fixed rate notes due in 2035 that was effective in March 2023. The new swap's floating receive leg exactly offsets the original swap's floating pay leg, resulting in a net fixed exposure.

In June 2023, Southern Gas Networks plc entered into a £550m committed bridging loan with three of its relationship banks. The bridging loan has an initial tenor of 12 months and the Company has the option to extend for a further 6 months thereafter. It has a floating drawn rate of interest based on SONIA plus a time-dependent margin. The bridge is intended to provide additional liquidity for Southern Gas Networks plc's refinancing requirements.

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023**31. RECONCILIATION OF PROFIT BEFORE TAXATION TO CASH GENERATED FROM OPERATIONS**

	2023	2022
	£m	£m
Profit before taxation	193	80
Depreciation charges	184	180
Loss on disposal of fixed assets	4	5
Amortisation of deferred income	(11)	(10)
Amortisation charges	23	22
Increase in provisions	10	-
Interest payable and similar expenses	274	195
Fair value movement on derivatives	1	73
Interest receivable and similar income	(17)	(7)
	661	538
(Increase)/decrease in trade and other debtors	(37)	9
Increase in trade and other creditors and employee benefits	74	1
Cash generated from operations	698	548

32. ANALYSIS OF CHANGES IN NET DEBT

	At 1.4.22	Cash flow	Other non-cash changes	At 31.3.23
	£m	£m	£m	£m
Cash				
Cash and cash equivalents	25	18		43
Short term deposits	55	155	-	210
	80	173	-	253
Debt				
Debts falling due within 1 year	(296)	308	(312)	(300)
Debts falling due after 1 year	(4,528)	(399)	187	(4,740)
	(4,824)	(91)	(125)	(5,040)
Derivative financial instruments				
Derivative financial assets	-	-	5	5
Derivative financial liabilities	(131)	-	15	(116)
	(131)	-	20	(111)
Total	(4,875)	82	(105)	(4,898)

SGN Midco Limited (Registered number: 11050000)

Notes to the Consolidated Financial Statements - continued
for the Year Ended 31 March 2023

33. OTHER NOTES TO THE CASH FLOW STATEMENT

In June 2022, the Group agreed to settle outstanding fees due in relation to certain guarantees provided by Assured Guarantee Corp. (as agent for Syncora Guarantee Inc.) and Assured Guarantee UK Limited that were previously in place over certain outstanding public bond instruments. The cash settlement amount of £9m is included within the "interest paid" line of the Consolidated Cash Flow Statement.

Included within the amount disclosed on the Consolidated Cash Flow Statement under Interest paid for 2022 is £4m in relation to the settlement of fees due to a prior guarantor of certain public bonds held by the Group (see note 6 for more details).

Included within the amount disclosed on the Consolidated Cash Flow Statement under Payments of mirror swaps for 2022 is £22m in relation to the termination of the Company's mirror swaps (see note 21 for more details).

34. MAJOR NON-CASH TRANSACTIONS

Other non-cash movements in borrowings relate to the amortisation of borrowing fees, loan accretion accruals and foreign exchange variances. Non-cash movements in derivative financial instruments relate to fair value movement and accretion accruals.