Northern Gas Networks Operations Limited

Annual Report and accounts
for the year ended 31 December 2011

Registered number: 3528783

The directors present their Annual Report on the affairs of the company, together with the accounts and auditor's report, for year ended 31 December 2011.

Principal activity

The principal activity of the company throughout the year was the provision of operations, maintenance and capital programme services for the North of England gas distribution network.

Business review

Operating profit for the year was £0.1m (nine months ended 31 December 2010 - £1.2m loss) as all costs plus a margin are recharged to Northern Gas Networks Limited ("NGN"). The tax charge for the year was £0.2m (nine months ended 31 December 2010 - £0.3m credit) largely as a result of prior period adjustments.

Business strategy

The company's purpose is to operate and maintain the North of England gas distribution network, so that it provides safe and secure gas supplies to the people and the businesses within the distribution network. The company's vision of success mirrors that of NGN, which is to be consistently benchmarked by the regulators, Ofgem and the Health and Safety Executive ("HSE") as being in the top two comparable utilities in safety management, efficiency and customer service.

Key performance indicators (KPIs)

The company is managed as part of the overall group. For this reason, the company's directors believe that further key performance indicators for the company are not necessary or appropriate for an understanding of the development, performance or position of the business. The performance of the group, including the company, is discussed in the Northern Gas Networks Holdings Limited Annual Report which does not form part of this report.

Environment

The company recognises the importance of its environmental responsibilities and undertakes its operations in an environmentally sensitive manner, complying with all relevant legislative requirements and higher standards where possible. The company is committed to the protection of the environment in the region it serves. The company's environmental management systems are certified under ISO 14001. This helps the directors deal proactively with future environmental issues and legislation and assist in the development of environmentally beneficial projects. In addition, NGN is the only gas distribution network which is accredited under both ISO 14001 and OHSAS 18001, in relation to health and safety management systems.

Principal risks and uncertainties

The company's principal risks and uncertainties are set out below.

Regulatory environment, revenue and costs

The gas industry is subject to extensive legal and regulatory obligations and controls with which the company must comply. The application and possible changes of these laws, regulations and regulatory standards could have an adverse affect on the operations and financial position of the company or in the case of financial misreporting, a potential fine.

Health and safety

There is a risk that an incident within the network leads to injury to an employee, contractor or a member of the general public. Any such incident could have an adverse affect on the reputation of the company, or lead to potential prosecution and reduced productivity.

Network performance

If the network assets were to fail it could result in a loss in supply of gas to customers and associated adverse publicity and an unexpected increase in costs.

Employees

The success of the company depends to a significant extent on the contribution of its employees and the employees of operational contractors. Fair and effective recruitment, training and employee development are critical to the successful functioning and progression of the business. The ability to adapt in a climate of change is dependent on the appointment and retention of a high calibre, competent, flexible, quality conscious and customer focused workforce all of whom are committed to business success and are given appropriate training. Appropriate succession planning strategies mean that development of existing staff is crucial. Effective resourcing and selection processes also play a positive role in improving the image of the company in the community it serves.

The company, as an equal opportunities employer, ensures that no job applicant receives less favourable treatment because of his or her age, colour, disability, ethnic or national origin, gender, marital status or sexuality or is disadvantaged by conditions or requirements which are irrelevant to performance and the company's needs.

Outlook

The directors expect the general level of activity to remain stable.

Financial risk management objectives and policies

The company's financial instruments comprise group borrowings, cash and various items such as trade debtors and trade creditors that arise directly from its operations. There are no key risks associated with these financial instruments as their main purpose is to finance the company's operations. The company does not hold or issue any derivative financial instruments for speculative purposes.

Going concern

The company's business activities, performance and position together with its principal risks and uncertainties likely to affect its future development and performance are set out on pages 1 and 2.

The directors have made enquiries and reviewed the forecasts, including sensitivity analysis, and in light of the facilities available, have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and accounts.

Dividends

The directors do not recommend payment of a dividend (nine months ended 31 December 2010 - £nil).

Directors

The directors, who served throughout the year except as noted, were as follows:

W Shurniak	(Chairman, resigned 28 June 2011)
A Hunter	(Chairman from 28 June 2011)
M J Horsley	(Chief Executive Officer, appointed 4 January 2011)
B Scarsella	(Chief Executive Officer, resigned 4 January 2011)
F R Frame	(resigned 21 November 2011)
H L Kam	
K S Tso	
N McGee	
M Robinson	
D Macrae	(appointed 21 June 2011)

Supplier payment policy

The company's policy is to settle terms of payment with suppliers when agreeing the terms of each transaction, ensure that suppliers are made aware of the terms of payment and abide by the terms of payment. Trade creditors of the company at 31 December 2011 were equivalent to 3 days' purchases, based on the average daily amount invoiced by suppliers during the year (nine month period ended 31 December 2010 – 9 days).

Charitable and political contributions

During the year the company made charitable donations of £nil (nine month period ended 31 December 2010 - £434), principally to local charities serving the communities in which the company operates. No political donations were made in the year (nine month period ended 31 December 2010 – £nil).

Disabled employees

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

Employee consultation

The company places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the company. This is achieved through both formal and informal meetings. Employees are consulted regularly on a wide range of matters affecting their current and future interests. Employees are eligible to receive an annual bonus related to the overall financial and operational performance of the company.

Auditor

Each of the directors at the date of approval of this report confirms that:

- so far as the director is aware, there is no relevant audit information of which the company's auditor is unaware; and

- the director has taken all the steps that he ought to have taken as a director to make himself 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 provisions of section 418 of the Companies Act 2006.

The directors will place a resolution before the annual general meeting to reappoint Deloitte LLP as auditor for the ensuing year.

1100 Century Way
Thorpe Park Business Park
Colton
Leeds
LS15 8TU

By order of the Board,

M J Horsley

Director

22 March 2012

Directors' responsibilities

The directors are responsible for preparing the Annual Report and accounts in accordance with applicable law and regulations.

Company law requires the directors to prepare accounts for each financial year. Under that law the directors have elected to prepare the accounts in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these accounts, the directors are required to:

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the accounts comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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To the Members of Northern Gas Networks Operations Limited

We have audited the accounts of Northern Gas Networks Operations Limited for the year ended 31 December 2011 which comprise the profit and loss account, the balance sheet, the statement of accounting policies and the related notes 1 to 16. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards ("United Kingdom Generally Accepted Accounting Practice").

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.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities statement, the directors are responsible for the preparation of the accounts and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Through management, the directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of accounts may differ from legislation in other jurisdictions.

Scope of the audit of the accounts

An audit involves obtaining evidence about the amounts and disclosures in the accounts sufficient to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the accounts. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited accounts. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on accounts

In our opinion the accounts:

- give a true and fair view of the state of the company's affairs as at 31 December 2011 and of its loss 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.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Directors' report for the financial year for which the accounts are prepared is consistent with the accounts.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where 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 accounts 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.

Christopher Powell FCA (Senior Statutory Auditor)
For and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Leeds, England

22 March 2012

Profit and loss account

For the year ended 31 December 2011

	Notes	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Turnover	1	173,244	140,591
Cost of sales		(173,144)	(140,846)
Gross profit (loss)		100	(255)
Other operating expenses	2	-	(953)
Operating profit (loss)		100	(1,208)
Finance charges (net)	3	3	(275)
Profit (loss) on ordinary activities before taxation	4	103	(1,483)
Tax on profit (loss) on ordinary activities	7	(187)	274
Loss for the financial year	13	(84)	(1,209)

The above results arise from continuing operations.

The accompanying notes are an integral part of this profit and loss account.

There are no recognised gains or losses in either the current year or prior period other than the loss for that period.

Balance sheet

31 December 2011

	Notes	31 December 2011 £'000	31 December 2010 £'000
Current assets			
Stocks	8	879	842
Debtors - due within one year	9	31,404	29,019
Cash at bank and in hand		798	138
		33,081	29,999
Creditors: Amounts falling due within one year	10	(32,233)	(28,869)
Net current assets		848	1,130
Provisions for liabilities	11	(920)	(1,118)
Net (liabilities) assets		(72)	12
Capital and reserves			
Called-up share capital	12	-	-
Profit and loss account	13	(72)	12
Shareholders' (deficit) funds	14	(72)	12

The accompanying notes are an integral part of this balance sheet.

The accounts of Northern Gas Networks Operations Limited, Registered number 3528783, were approved by the Board of Directors and authorised for issue on 13 March 2012 and signed on its behalf by:

M J Horsley Director

22 March 2012

The principal accounting policies are summarised below. They have all been applied consistently throughout the year and the preceding period.

Basis of accounting

The accounts have been prepared under the historical cost convention and in accordance with applicable United Kingdom ("UK") accounting standards.

The company is exempt from the requirement of FRS1 (revised) "Cash flow statements" to present a cash flow statement as it is a wholly owned subsidiary of Northern Gas Networks Holdings Limited, which prepares consolidated accounts which are publicly available.

Going concern

The Directors' report includes a note on page 3 stating that the directors consider the business to be a going concern at the time of the approval of the Annual Report and accounts.

Stocks

Stocks are stated at the lower of cost and net realisable value. Provision is made for obsolete or defective items where appropriate.

Taxation

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

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

A net deferred tax asset is regarded as recoverable and therefore recognised only when, 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 at the average UK tax rates that are expected to apply in the years in which the timing differences are expected to reverse, based on UK tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a non-discounted basis.

Turnover

Turnover represents income receivable for the provision of services to NGN net of Value Added Tax.

Pension costs

Employees of the company participate in either the Northern Gas Networks Limited Pension Scheme, a defined benefit scheme which is now closed to new entrants or defined contribution pension schemes operated by NGN. The amount charged to the profit and loss account in respect of pension costs 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.

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, except where the period to the review date on which the rent is first expected to be adjusted to the prevailing market rate is shorter than the full lease term, in which case the shorter period is used.

1 Segment information

The directors consider that the company has only one class of business. The company's turnover is generated wholly from within the UK.

2 Other operating expenses

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Administrative expenses	-	(953)

3 Finance charges (net)

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2011 £'000
Interest receivable	3	-
Interest payable to group undertakings	-	(275)
	3	(275)

4 Profit (loss) on ordinary activities before taxation

Profit (loss) on ordinary activities before taxation is stated after charging:

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Operating lease rentals – other	686	128
Fees payable to the company's auditor for the audit of the company's annual accounts	24	35

Fees payable to Deloitte LLP and their associates for non-audit services to the company are not required to be disclosed because the consolidated accounts of the parent company disclose such fees on a consolidated basis.

5 Staff costs

The average monthly number of employees (including executive directors) was:

	Year ended 31 December 2011 Number	Nine months ended 31 December 2010 Number
Operations	1,139	1,102

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Their aggregate remuneration comprised:		
Wages and salaries	40,179	30,809
Social security costs	3,820	2,450
Pension costs	7,629	5,499
	51,628	38,758

6 Directors' remuneration and transactions

Remuneration

The remuneration of the directors was as follows:

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Emoluments	-	82

In the current year, all directors of the company were remunerated by fellow group companies and not recharged.

The total remuneration received by the directors during the year was £454,000 (2010 - £822,000).

6 Directors' remuneration and transactions (continued)

Pensions

The number of directors who were members of pension schemes was as follows:

	Year ended 31 December 2011 Number	Nine months ended 31 December 2010 Number
Defined benefit scheme	-	1

Transactions

There have been no transactions with directors in the year (nine month period ended 31 December 2010 – £nil) other than as set out above in respect of remuneration.

7 Tax on profit (loss) on ordinary activities

The tax charge (credit) comprises:

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Current tax		
UK corporation tax	27	(313)
Adjustments in respect of prior period	160	-
Total current tax charge (credit)	187	(313)
Deferred tax		
Current period - origination and reversal of timing differences	-	39
Total deferred tax	-	39
Total tax on profit (loss) on ordinary activities	187	(274)

7 Tax on profit (loss) on ordinary activities (continued)

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

	Year ended 31 December 2011 £'000	Nine months ended 31 December 2010 £'000
Profit (loss) on ordinary activities before tax	103	(1,483)
Tax on profit (loss) on ordinary activities at standard UK corporation tax rate of 26.5% (nine month period ended 31 December 2010 – 28%)	27	(415)
Effects of:		
Expenses not deductible for tax purposes	-	90
Depreciation in excess of capital allowances	-	1
Other timing differences	-	11
Adjustments in respect of prior period	160	-
Current tax charge (credit) for the year	187	(313)

The company earns its profits in the UK. Therefore the tax rate used for tax on profit (loss) on ordinary activities is the standard rate for UK corporation tax, currently 26.5% (nine month period ended 31 December 2010 – 28%).

8 Stocks

	31 December 2011 £'000	31 December 2010 £'000
Raw materials	879	842

There is no material difference between the balance sheet value of stocks and their replacement cost.

9 Debtors – due within one year

	31 December 2011	31 December 2010
	£'000	£'000
Trade debtors	326	2,609
Amounts owed by group undertakings	27,257	21,431
Prepayments and accrued income	847	905
VAT	2,705	4,074
Other debtors	269	-
	31,404	29,019

10 Creditors: Amounts falling due within one year

	31 December 2011	31 December 2010
	£'000	£'000
Trade creditors	1,553	3,404
Other taxation and social security	1,197	1,377
Accruals and deferred income	29,483	24,088
	32,233	28,869

11 Provisions for liabilities

	Contractor Claims
	£'000
At 1 January 2011	1,118
Credited to profit and loss account	(101)
Utilised in the year	(415)
Released unused	(432)
Transferred from accruals	750
At 31 December 2011	920

Contractor claims

The provision for contractor claims relates to claims received from primary contractors in respect of work variations and final invoice valuations upon closing out contracts and represents the best estimate of the amounts required to settle these claims, which is expected mainly within one year of the balance sheet date.

12 Called-up share capital

	31 December 2011 £	31 December 2010 £
Allotted, called-up and fully-paid		
2 ordinary shares of £1 each	2	2

13 Reserves

	Profit and loss account £'000
At 1 January 2011	12
Loss for the financial year	(84)
At 31 December 2011	(72)

14 Reconciliation of movements in shareholders' funds (deficit)

	31 December 2011 £'000	31 December 2010 £'000
Loss for the financial period	(84)	(1,209)
Capital contributions	-	19,118
Net movement in shareholders' (deficit) funds	(84)	17,909
Opening shareholders' funds (deficit)	12	(17,897)
Closing shareholders' (deficit) funds	(72)	12

On 27 October 2010, prior to the sale of the company to NGN, the previous ultimate parent company, United Utilities plc waived £17.3m of the borrowings owed to it by the company under its group cash pool arrangements by way of a capital contribution.

Subsequent to the acquisition, NGN provided funding to the company to settle its outstanding liabilities by way of a further capital contribution of £1.8m.

15 Financial commitments

The company had no capital commitments at the end of the financial year (31 December 2010 - £nil).

Annual commitments under non-cancellable operating leases are as follows:

	31 December 2011 £'000	31 December 2010 £'000
Expiry date:		
- within one year	66	73
- between two and five years	529	450
	595	523

16 Ultimate controlling party

The directors regard Northern Gas Networks Holdings Limited, a company incorporated in England and Wales, as the ultimate parent company and the ultimate controlling party. Northern Gas Networks Limited is the immediate parent company.

Northern Gas Networks Holdings Limited is the parent company of the largest and smallest group of which the company is a member and for which group accounts are drawn up. Copies of the accounts are available from 1100 Century Way, Thorpe Park Business Park, Colton, Leeds, LS15 8TU.

The Shareholders of Northern Gas Networks Holdings Limited are a consortium comprising of:

PG (April) Limited (47.1%)
Beta Central Profits Limited (41.3%)
SAS Trustee Corporation (11.6%)

As a subsidiary undertaking of Northern Gas Networks Holdings Limited, the company has taken advantage of the exemption in FRS 8 “Related party disclosures” from disclosing transactions with other members of the group headed by Northern Gas Networks Holdings Limited.