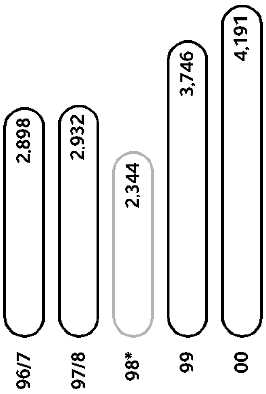
POWERGEN

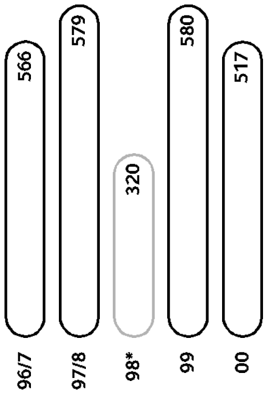
Powergen Report 2000

Financial highlights

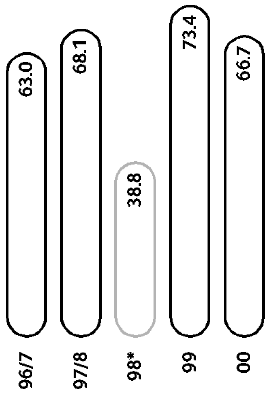


Turnover
£ millions

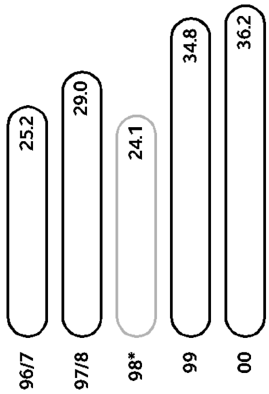
* Nine months ended December 1998



Pre-exceptional profit before goodwill amortisation and tax
£ millions



Pre-exceptional earnings per ordinary share[2]
pence



Dividends per ordinary share
pence

> Profits £517 million[1] and earnings 66.7 pence per share[2]
> Dividend up 4% to 36.2 pence per share
> Strategic re-direction to an Anglo American business
> Announced asset sales exceeding £1,000 million

1 Before tax, exceptional items and goodwill amortisation
2 Before exceptional items and goodwill amortisation

		Year ended 30 March 1997	Year ended 29 March 1998	Nine months ended 3 January 1999	Year ended 2 January 2000	**Year ended 31 December 2000**
Group turnover	£m	2,898	2,932	2,344	3,746	**4,191**
Pre-exceptional profit before goodwill amortisation and tax [3]	£m	566	579	320	580	**517**
Profit/(Loss) before tax [1, 3]	£m	568	210	(245)	762	**468**
Earnings per ordinary share [2, 3]	pence	63.0	68.1	38.8	73.4	**66.7**
Dividends per ordinary share	pence	25.2	29.0	24.1	34.8	**36.2**
Dividend cover per share [2, 3]	times	2.5	2.3	1.6	2.1	**1.8**
Net assets [3]	£m	2,022	1,656	1,345	1,984	**2,286**
Net debt	£m	655	481	2,408	2,024	**5,322**
Shares in issue (year end)	millions	637.4	644.5	649.1	649.7	**651.5**
Staff numbers (year end)		3,551	3,453	8,118	7,678	**11,742**

Notes

1 In the year ended 31 December 2000, profit before tax includes exceptional credits (net) of £26 million. In the year ended 2 January 2000, profit before tax includes exceptional credits (net) of £250 million. In the nine months ended 3 January 1999 profit before tax includes exceptional costs of £537 million. In the years ended 29 March 1998 and 30 March 1997, profit before tax includes exceptional costs of £369 million and exceptional credits of £2 million respectively.

2 Earnings per share (eps) and dividend cover figures quoted above are based on profits before exceptional items and goodwill amortisation. After charging or crediting exceptional items and goodwill amortisation, the figures are: year ended 31 December 2000 eps 65.9p; year ended 2 January 2000 eps 109.0p; nine months ended 3 January 1999 eps (24.1)p; year ended 29 March 1998 eps (19.5)p and year ended 30 March 1997 eps 63.3p.

3 Profit before tax, earnings per share and net assets for the two years ended 29 March 1998 were restated following the adoption of Financial Reporting Standard 12 from 30 March 1998.

The Group

UK

Powergen is one of the UK's leading integrated electricity and gas companies, and one of the country's best known energy brands.

Its UK operations are split into five main activities;

> Selling electricity, gas and other essential services, with over three million residential, business and industrial customer accounts.

> Trading electricity, gas, oil and coal.

> Producing electricity from a portfolio of world-class power stations.

> Distributing electricity to 2.4 million homes and businesses in the East Midlands.

> Providing highly efficient combined heat and power plant to meet the electricity and steam needs of energy-intensive businesses.

US

LG&E Energy is a diversified energy services company with businesses in power generation, retail gas and electric utility services, asset-based energy marketing and project development.

Its regulated businesses are:

> Louisville Gas and Electric Company, a gas and electricity utility, serving customers in 17 Kentucky counties; and Kentucky Utilities Company, an electricity utility serving 77 Kentucky counties and five counties in Virginia. Together, these utilities serve over one million customer accounts.

Its unregulated businesses include:

> 50 per cent interests in an operational plant in Texas and one under construction in Georgia.

> Western Kentucky Energy, a wholly-owned subsidiary, which operates and leases four coal-fired plants owned by Big Rivers Electric Corporation in Western Kentucky.

> Interests in three Argentinian gas distribution companies.

Powergen International

Outside the UK, Powergen has built an international power generation business, with power projects in Europe, India and Asia Pacific. As part of a strategic refocusing of the Group onto the UK and US markets, agreement has been reached for the sale of the majority of these assets. Powergen is retaining a 20 per cent interest in the joint venture companies acquiring its Australian, Indian and other Asian assets.

Chairman's statement

Powergen has shown once again its ability to adapt successfully to new challenges and new working environments. We completed our acquisition of LG&E Energy Corp. (LG&E) and, through our value delivery process, we have identified higher than anticipated cost savings. We will exceed our £1 billion debt reduction target from the announced sales of assets in the UK and overseas. And we have achieved all of this without losing focus on our UK business whose performance has underpinned our solid results for this year. Overall, we have either met, or exceeded, all of the objectives that we set for ourselves last year. Powergen has transformed itself during the year 2000 into a business well positioned to take advantage of opportunities that will arise from the developing competitive markets in the UK and the US.

Group turnover for the year was £4,191 million, up £445 million on last year, largely due to increased turnover in our businesses in the UK and overseas. We also had three weeks' contribution from LG&E. Profit before tax, exceptional items and goodwill amortisation was £517 million compared with £580 million in the same period in 1999.

Earnings per share on a similar basis were 66.7 pence, compared to 73.4 pence last year. After £75 million of goodwill amortisation (£68 million last year) profit before tax and exceptional items was £442 million. There were a number of exceptional items during the year, netting out to £26 million, which related to asset disposals and write-downs, bond buybacks and the acquisition of LG&E.

The Board has declared a final dividend for the year of 25.4 pence, making the total dividend 36.2 pence per share, which represents a year on year increase of 4 per cent. This dividend will be paid on 30 March 2001 to shareholders on the record on 2 March 2001.

As previously announced at the time of our interim results in September, we will now report our results and pay dividends on a quarterly basis. This will take effect from the first quarter 2001. We would expect to pay 25 per cent of the previous year's dividend in each of the first three quarters of the year with any adjustment coming in the fourth quarter. This move to quarterly dividends will benefit shareholders and lead to a smoothing of dividend payments throughout the year.

UK

Our UK business performed ahead of expectations last year. Our integrated approach continued to deliver value, confirming that this is the correct model for the UK market in today's competitive environment. Our retail business passed the three million customer account mark, providing profitable growth through our simple retail strategy of "getting more customers and selling more products". Energy trading continued as the hub of our integrated business, co-ordinating our market actions and maximising the value of our generation and customer assets. Our production business provided low cost generation giving flexible options to our energy trading business. And in distribution, we are nearing completion of our cost saving initiatives, proving that our asset management skills are just as relevant in distribution as they are in generation. All of these businesses contribute to our diversified UK earnings base.

Electricity prices stabilised in the second half of 2000 with annual baseload contracts being struck at around £19/MWh. Powergen's hedging policy meant that the impact of lower prices from February 2000 only started to have a material impact in the fourth quarter of 2000. These lower prices will impact for the whole of 2001. Higher gas prices will have a small effect on profits. Powergen's generation output and gas costs are largely hedged through 2001. However, this position will move throughout the year and we will take opportunities to secure additional value as they arise.

The New Electricity Trading Arrangements (NETA) are scheduled for introduction on 27 March 2001. For Powergen, with our flexible generation, growing customer base and integrated trading strategy, NETA represents a business opportunity rather than a threat.

With our strong national brand we will continue to build on the successes of our winning retail business. We exceeded our three million customer account milestone late in 2000 and now have the products and sales infrastructure to achieve our target of five million by the end of 2002. Our focus for 2001 in the residential market will be to continue to grow our customer base organically, whilst ensuring we retain our existing customers and cross sell new products to them. The Small & Medium Enterprise (SME) market continues to be our fastest growing and most profitable retail business segment achieving 53 per cent growth during the year. We will continue to focus on this section of the market and move away from some of the less profitable high volume business that has been our traditional retail base.

US

Across the Atlantic, we completed our acquisition of LG&E on 11 December. Although the transaction took just over nine months to close, we were able to spend the time before completion working with LG&E to benchmark their business against world's best practice. Efficiency improvements, to be delivered over the next three years, will be greater than initial expectations and LG&E has already announced a voluntary severance package. Initial indications are that the take up for this package will be good, with staff reductions to be phased in to ensure no loss of service quality. Operationally, LG&E has had a good year in both the regulated utility operations of LG&E and Kentucky Utilities (KU), and in their unregulated businesses.

The acquisition of LG&E cost £2,258 million and created goodwill of £1,498 million. As a result gearing, defined as debt as a proportion of total capital, increased to 70 per cent at the year end.

Asset sales

Having set ourselves a target of reducing debt by £1 billion through the sale of assets in the UK and overseas, I am pleased to report that we will exceed this sum. Overall the asset sale programme is on target to reduce debt by around £1.25 billion. We have decided to retain Connah's Quay in the UK and are still reviewing the options for our assets in Germany and Hungary. All of the announced sales are on target to complete during the first half of 2001.

Strategy

Powergen has a clear strategy for the UK and US that gives us the 'Best of both worlds'.

Our UK business strategy has three key steps: first, to sustain and develop the asset businesses. The value of our generation assets can be sustained through our energy trading activities and by maintaining our focus on world class asset management. We will also develop our asset businesses by using our world class skills to manage distribution and generation assets not necessarily owned by Powergen. The second step is to build competitive trading and retail businesses. This is essential if we are to take advantage of increasing competition in wholesale and retail markets. Competitive risk management and trading skills are required to maximise the value of our generation assets balanced with contracts delivered from our competitive retail business which is itself a source of significant potential value. The third step is to export our UK competencies to support Powergen in both the UK and Europe. This is vital if we are to succeed with our group strategy of using our UK experience from managing liberalisation of this market to gain a competitive edge in the deregulating US market.

Our US business strategy takes a different route. First, over the next three years, LG&E has to deliver the cost savings identified through our value delivery process to move them towards world's best practice. Next will be to reorganise the business into its component parts and, to give the business a more commercial focus, create a trading hub to maximise margins and manage risks across the group. Finally, LG&E must provide the platform for the group's overall US strategic ambitions of growing through M&A in the midwest region.

In addition to our strategies for the UK and the US, we also have two other priorities for 2001. The first is to complete our announced asset sales. The second is to focus on ways of reducing the cost of our debt, both through lowering the interest cost and reducing in absolute terms the amount of group debt.

We are confident that this strategy will deliver real value to our shareholders. This strategy is in place and we are focused on its delivery.

Board and Management

With the Group well positioned for the future, I feel that now is the right time for me to take a step back from the business and, as part of a planned succession, Nick Baldwin succeeded me as chief executive on 21 February 2001. Nick, as an executive director of Powergen, has successfully run our UK business since February 1998 and has been with Powergen in a number of roles since our formation in 1989. I shall remain chairman of the Board of Powergen.

The latter part of the year also saw a number of changes to the Board. In December, we announced that Tony Habgood would be standing down at the end of January 2001. Tony served as a non-executive director for eight years, and I have always personally valued his contribution to the running of the business.

As part of the acquisition of LG&E, Roger Hale joined the Board on 11 December 2000 at the time of its completion. Roger subsequently decided to stand down with effect from 30 April 2001. Whilst I have only known Roger for a short time, I have admired his professionalism in the period we worked together, both during the negotiation of the transaction and subsequently.

I wish both Tony and Roger every success for the future.

Vic Staffieri will be joining the Board with effect from 30 April 2001 as chief executive officer of LG&E, and I know he will play a major part in implementing Powergen's American strategy.

I have already said that this has been one of Powergen's most challenging years and I know this has been felt by all employees. I would firstly like to welcome all LG&E employees to the Powergen Group, and secondly to record, on my own behalf and that of the Board, our thanks to all employees for the magnificent contribution they have made during the year.

Ed Wallis, chairman

Operating review

Powergen's vision is to create one of the world's leading integrated electricity and gas businesses.

In 2000, it achieved a strategic redirection of the Group into an Anglo-American energy company with the $3.2 billion acquisition of LG&E Energy Corp. (LG&E), a vertically-integrated energy group based in Louisville, Kentucky.

Powergen also announced that it would be offering for sale selected UK and international assets to reduce its debt by £1,000 million. Together, these moves have refocused the Company's activities on the UK and US energy markets, and provide it with a lower risk, higher quality and more diversified earnings base with a reduced dependency on profits from UK generation.

UK business

Powergen is one of the UK's leading integrated electricity and gas companies, with a business built on:

- marketing electricity, gas, telecoms and other essential services to domestic and business customers
- asset management in electricity production and distribution
- energy trading, to support these activities.

Its UK strategy is to sustain and develop its asset businesses, build competitive trading and retail businesses, and to export its competencies to support Powergen's activities outside the UK.

Retail

Targets achieved Powergen continued to deliver profitable growth in the three segments of its retail business: residential, small and medium enterprises (SMEs) and corporate clients. By the end of the year, it had reached its target of over three million customer accounts – an increase of 17 per cent on the 1999 year end figure of 2.6 million. This success is due to a targeted marketing strategy and a wider product range. In addition, the business continued to focus on its cost base to improve margins by using lower cost sales channels and implementing systems to reduce back office costs. Operating profit for the year increased as improved margins and increases in customer numbers more than offset increased marketing spend and costs associated with signing up new customers.

Residential and SME customers The residential business grew by 13 per cent to 2.7 million customer accounts during the year. SME customer accounts increased by 53 per cent to 317,000 accounts, making it the industry's fastest growing retail business in this sector.

During the year, Powergen successfully expanded the range of products it offers to establish itself as a provider of essential services to customers in the residential and SME markets. In February, it announced its joint venture with Affinity Internet Holdings, an internet and telecommunications company, to develop internet products, fixed and mobile telecommunications services, and a convergent billing system enabling multiple products to be detailed on a single bill. The joint venture enabled the Company to launch fixed-line telephone services products for residential and SME customers, for which it had achieved 120,000 and 13,000 accounts respectively by the year-end. A mobile telephone service is currently being market tested. Convergent billing will be introduced during 2001.

The Company also joined forces with Alto Digital to offer website development packages to SME customers.

In July 2000, Powergen and Legal & General announced a pilot scheme enabling Powergen to support its customers by offering a range of cost-effective financial services, and providing Legal & General with a low cost way to reach a substantial customer base with its products. This has been successful and a full launch is now imminent.

New electricity products launched specifically for the residential market during the year include GreenPlan and No Standing Charge tariffs.

Large business In the large business sector, Powergen built further on its market leadership position in the sale of electricity, and consolidated its position as one of the leading gas suppliers in the market, with annualised sales of 21TWh of electricity (representing a 10 per cent growth in sales) and 23TWh of gas (a 20 per cent growth).

The business is continuing to develop innovative energy services to help its customers manage the conditions in the energy market, with current efforts heavily focused on the impact of the new electricity trading arrangements (NETA).

After the year end, Powergen announced that it is investing in a joint venture, to be called Acertus, with Accenture (formerly Andersen Consulting) to offer on-line energy management services to large pan-European companies. Acertus will be run independently from both parent companies.

Looking ahead, Powergen has reviewed its strategy in this sector in the light of its reduced output following the sales of Cottam and Rye House power stations. In future, it will focus on providing services to customers offering improved margins in place of higher volume, low margin customers.

Future growth Powergen has a target of increasing its customer base to five million accounts by the end of 2002. Over 50 per cent of the Company's new customers are gained by telemarketing. Two new telemarketing centres were opened in 2000, one in Dearne Valley in South Yorkshire and another at Tannochside near Glasgow, both of which are already exceeding targets. Telemarketing is complemented by targeted direct mail and advertising, a selective use of face-to-face sales, third party relationships and the internet. In addition to gaining new customers, the Company is focusing on reducing its losses of customers to other suppliers.

Energy trading

The hub of the UK business Energy trading is the hub of Powergen's integrated UK business, co-ordinating its market actions and maximising the value from its generation and customer assets. The Company's integrated trading strategy lessened the impact of both lower wholesale electricity prices and the loss of volume following the sale of Fiddler's Ferry and Ferrybridge power stations in 1999.

Electricity prices continued their downward trend during the year. The underlying levels of System Marginal Price in the electricity Pool show a year-on-year fall of some 16.1 per cent and, even with higher levels of capacity payments, the Pool Purchase Price was 3.3 per cent lower than during 1999.

Withdrawal of plant, fragmented maintenance programmes and instances of unplanned outage led to periods of tightness in the capacity margin. Powergen anticipated this well and had the plant available to pick up additional market share. The business took advantage of opportunities to secure additional value by asset-based energy marketing in the short-term electricity and gas markets to optimise its portfolio position.

High gas prices during the year have changed the economics of electricity generation. As a generator with a flexible plant portfolio, Powergen is able to switch from gas to coal without impact on its market share.

For 2001, Powergen is largely hedged in its electricity and gas portfolios. The Company will again trade around these positions as opportunities arise to secure additional value.

New Electricity Trading Arrangements The implementation of NETA, originally scheduled for 2000, was postponed to 27 March 2001 following problems with the testing of the new central industry systems. NETA will not change the fundamental electricity demand/supply balance in the UK, but will change the market structure and deliver more transparency and better risk apportionment between participants. Powergen is confident that the shape and flexibility of its UK business leaves it well placed to manage the new challenges of NETA and over the last two years has been preparing for its introduction to ensure that it has the systems and people in place. It has also developed a Control and Governance framework for its trading operations, which gives traders operational freedom within a closely defined framework, whilst providing robust control and risk management for the increasingly dynamic NETA environment.

Generation

High plant availability During the year, the total electricity demand in England and Wales rose by 2.2 per cent to 301.6TWh. The high availability of Powergen's plant, together with an increase in outages from competitors, enabled it to generate 43.2TWh – a market share of 14.3 per cent (1999: 15.9 per cent; 1998: 18.5 per cent). This is slightly higher than the generation it achieved from the same plant in 1999. Powergen expects that its output will reduce to 30TWh in 2001 as a result of plant disposals, with market share falling to around 10 per cent.

Changes to the portfolio Powergen made some significant changes to its plant portfolio during the year. As part of its asset sale programme, it completed the sale of the 2,000MW coal-fired Cottam power station for £398 million in December 2000. Also in December, it announced that it had reached agreement for the sale of the 715MW combined cycle gas turbine (CCGT) plant at Rye House for £220 million. This sale is expected to be completed in the first quarter of 2001.

In September 2000, Powergen completed the purchase of a 50 per cent share in Corby Power Limited for a net consideration of £34 million. Corby Power owns a 350MW CCGT plant, whose output is already purchased by Powergen under a long-term contract.

Following the completion of the sale of Rye House, Powergen will have 7.5GW of wholly-owned generation plant in the UK, which includes 3.5GW of coal-fired plant and 2.3GW of gas-fired plant. This balanced portfolio gives the Company the flexibility to respond to changes in the marketplace.

Future growth Powergen aims to build on its existing strengths in electricity production by developing a comprehensive asset management service for generation plant owners in the UK and elsewhere in Europe. The integrated service will comprise operations and maintenance, technical consultancy and risk management.

Generation licence conditions Following an eight-month inquiry, the Competition Commission decided not to give the go-ahead to Ofgem's decision to include a 'market abuse' clause in the generation licences of two UK generators. In the light of the Competition Commission's decision, Ofgem agreed to withdraw the licence condition from the licences of the generators who had previously accepted it, including Powergen, who accepted the condition on the understanding that the Competition Commission's findings would be reflected in its own licence.

Combined heat and power

Continued growth in CHP Powergen's combined heat and power (CHP) business has continued to grow, sustaining its position as a leading provider of industrial CHP in the UK. Its portfolio currently comprises 484MWe of operational projects for clients ranging across a number of sectors, including pharmaceuticals, chemicals, paper and oil-refining.

In August, the Company successfully commissioned one of the UK's largest CHP plants. The 130MWe and 400MWth project, at Winnington in Cheshire, was completed both on schedule and within budget.

Two new projects were announced during the year, with a combined investment of £60 million:

- a 56MWe and 40MWth CHP plant in Stoke-on-Trent, due for commercial operation at the end of 2001
- a new 24MWth fluidised bed combustion plant at the Kemsley Paper Mill in Kent, which will be fully integrated with Powergen's existing CHP plant on the site. This plant is expected to become operational in summer 2002.

Powergen has also achieved exclusivity agreements on a number of other schemes offering a further potential 60MWe.

Investment in renewable energy Powergen Renewables, a joint venture with the Abbot Group, is one of the UK's leading developers and owner/operators of wind farms. It has interests in 14 operational onshore wind farms in the UK and Eire with a total capacity of 78MW.

This portfolio includes the UK's first offshore wind farm, a 4MW development at Blyth off the Northumberland coast, which was commissioned in December 2000.

In addition to the operational sites, construction work is underway on a 15MW wind farm in Northern Ireland. Powergen Renewables also has 200MW of development projects that have either planning consents or energy sales contracts in place.

Distribution

Driving distribution to world's best practice The distribution business, East Midlands Electricity (EME), performed well during the year, despite the severe storms which affected the East Midlands region in October.

Operating profit fell as a result of the impact of the third distribution pricing review and one-off costs related to the sale of the metering business, offset by cost savings within the business.

The business is ahead of schedule in its drive to reduce costs and achieve world's best practice. It has now rationalised its operational structure to one central headquarters supported by four field operating centres. It is also on track to deliver £75 million of revenue and cash cost savings per year through achieving a 50 per cent reduction in employee numbers and outsourcing 50 per cent of business services to contractors.

Following its decision that metering and contracting were non-core activities best run by external service providers, Powergen completed the sale of the EME contracting business in February 2000. The terms of the sale include a three-year agreement under which the buyer will provide service support to the Company. After the year-end, Powergen also announced the sale of its metering business (excluding its non half-hourly meter assets), which will allow this business to grow as a national player providing cost-effective services back to the distribution business.

Business separation The Utilities Act 2000 requires the separation of distribution and supply activities into separate legal entities (although they may still be within the same group) by a date to be fixed (currently expected to be in July 2001). Powergen has been supportive of the process of business separation, having previously agreed with Ofgem a plan to ensure the independence of the distribution business. A large proportion of this plan is now implemented, with completion due in the first quarter of 2002.

Powergen International

Powergen International Ltd (PGI) is a wholly-owned subsidiary of Powergen, responsible for the Company's power projects in Europe, India and Asia Pacific.

PGI performance Operating profit from PGI increased in 2000. Profits from GPEC, which owns the Paguthan plant in India, increased significantly, reflecting the increase in Powergen's stake in the project from 74.1 per cent to 88 per cent during the period. However, industrial relations problems at Yallourn power station in Australia (in which Powergen held a 49.95 per cent stake) led to a £10 million drop in profits from that business, despite some recovery in Pool prices earlier in the year.

In Hungary, the Company's 100 per cent-owned Csepel II plant entered full commercial operation in November, to time and budget. The 389MW CCGT is the first privately-financed energy production facility in Hungary. Also in November, full commissioning was achieved at the 1,220MW coal-fired plant at Paiton in Indonesia, in which Powergen holds a 35 per cent stake. Both plants are performing in line with expectations.

Disposals agreed In the fourth quarter of the year, Powergen made a number of announcements relating to the disposal of selected international assets.

In October, it completed the sale of its 49.9 per cent shareholding in the 528MW Korean power project, LG Energy, for £35 million.

In December, it announced an agreement to sell its Australian, Indian and other Asian assets to companies that will be managed and 80 per cent owned by CLP Power International. Powergen will retain a 20 per cent equity stake in these companies, which will acquire:

- in India, all of Powergen's interests including its 88 per cent stake in GPEC and its development projects
- in Australia, Powergen's 49.95 per cent stake in the 1,450MW coal-fired Yallourn power station, along with 42.05 per cent of the shares held by other shareholders
- in Thailand, Powergen's 50 per cent interest in BLCP, the company developing a coal-fired power station at Map Ta Phut.

Through this deal, Powergen will receive £286 million in cash and achieve a total debt reduction of £458 million. The new companies set up under the agreement with CLP may acquire the Company's interest in Paiton within the next five years, subject to a number of conditions. Completion of the Australian part of the deal was achieved in February 2001.

Powergen also announced in December an agreement to sell its 49.9 per cent shareholding in Turbogas, a private joint venture that owns a 990MW CCGT plant at Tapada do Outeiro in Portugal.

The Company is reviewing its options in respect of its remaining European interests: the Csepel I and Csepel II plants in Hungary, a 33 per cent share in the MIBRAG mining complex in Germany and a 22 per cent share in the Schkopau power station in Germany.

US business

Powergen achieved its goal of entering the US energy market through the acquisition of LG&E, a Kentucky-based diversified energy services company with businesses in power generation, retail gas and electric utility services, asset-based energy marketing and project development. On a US GAAP standalone basis, LG&E's total operating profit for 2000 was $497 million. The group employed 5,343 people at the year end.

The acquisition was completed on 11 December, within the anticipated 9- to 12-month approval timetable. For the 21 days that it was part of the Powergen Group, it contributed £8 million to operating profit.

Going forward, Powergen's US strategy is to deliver cost savings at LG&E, to reorganise the business into its component parts with an increased commercial focus, and to use it as a platform from which to grow in the US Midwest.

Business operations LG&E operates two utility businesses that are regulated in Kentucky by the Kentucky Public Services Commission and in Virginia by the Virginia State Corporation Commission. These serve over one million electricity and gas accounts over a transmission and distribution network covering some 70,000 square kilometres. LG&E also operates a number of unregulated businesses, which include unregulated generation in the US and gas distribution in Argentina.

Value delivery Prior to the completion of the deal, Powergen and LG&E worked together to benchmark LG&E's operations against world's best practice, explore the scope for efficiency gains, and prepare for the integration of LG&E into Powergen. The results of this work have been built into LG&E's business plan for 2001, with recognised scope for savings to take it to improved levels of efficiency in generation and distribution.

LG&E will maintain its headquarters in Louisville, Kentucky, which will now serve as the headquarters for Powergen's US operations.

Other activity

Managing the property portfolio Powergen Property continued to focus on the estate management of the Group's property portfolio and the sale of its surplus sites. It drew further income from the UK portfolio, principally through early disposal of the remaining plots on the Company's site at Hams Hall in the West Midlands. Agreement was also reached with Leicester City Football Club for the sale of the town's former power station site for the construction of the club's new stadium.

Eighteen of the 27 sites vacated during the re-organisation of the distribution business were sold. The development of the new EME headquarters and four field operating centres was completed on schedule.

Technology Powergen's technical development activities, carried out at its Power Technology Centre, are focused on supporting the Company's main business objectives, providing innovative services and products, and developing profitable new income streams.

During 2000, these activities were primarily in support of generation, but also increasingly for the benefit of gas and

electricity distribution and the energy trading and retail businesses. This work included:
- developing market models and trading tools to help the Company prepare for NETA
- reducing the costs of the repair and replacement of generation plant components
- developing strategies for minimising the environmental impact and improving the operational performance of the distribution business.

Power Technology also carries out contract research and development as part of its portfolio of technical support for external customers. It is an active participant in UK and European research programmes aimed at developing advanced, cleaner and more efficient power plant.

Environmental performance Powergen continued its work to minimise the impact of its operations on the environment during 2000.

The Company holds corporate certification under the international environmental management standard ISO 14001 for its electricity production, gas operations and associated services. The distribution business is continuing to work towards achieving full certification by the end of 2001. Work has begun to extend the implementation of ISO 14001 to Powergen's US subsidiaries.

The Company's emissions of sulphur dioxide and oxides of nitrogen from its UK power stations in 2000 remained well below the targets set by the Environment Agency. Emissions of carbon dioxide also remained well below internal targets.

Powergen was not subject to any environmental prosecutions from the Environment Agency during the period, and so retaining its record of zero prosecutions for an environmental offence.

The Environment Agency issued final power station-specific sulphur dioxide limit authorisations after the year-end, which are in line with the levels discussed during the consultation period. The Company is working to meet the improvement programme conditions in these authorisations. Discussions on future limits for oxides of nitrogen are now underway.

The 2000 Business in the Environment survey of environmental engagement and performance ranked Powergen 51st out of the FTSE 350 companies taking part. This fall from the Company's previous position of 12th reinforced the need for continual improvement and further challenging targets in all areas.

Employees The number of employees in the Group increased from 7,678 to 11,742, reflecting changes in the UK business and the acquisition of LG&E at the end of 2000.

A new framework for collective bargaining was implemented, reflecting the diverse nature of the Company's activities and providing for a shift towards a more business-focused approach.

Two major business areas in the UK achieved Investors in People accreditation for the first time in 2000, joining the increasing numbers of Powergen business units with the award.

A number of graduates were recruited onto the Company's graduate development programme through an internet-based process.

During August 2000, a sample of around 900 employees from Powergen and LG&E participated in a telephone-based survey to evaluate the feelings of employees towards the merger of the two companies in order to identify and respond to key areas of concern.

Work began on the alignment of a number of employee-related activities between the UK and the US during the latter half of 2000. In particular, nominations onto career development centres, which feed into the planning process for progression to key positions, have been widened to include US participants.

Commitment to health and safety Despite significant organisational change, Powergen maintained its uncompromising approach to the effective management of health and safety during 2000 and continued to achieve world class standards of health and safety performance.

Public endorsement of the Company's safety culture came with the award of the Royal Society for the Prevention of Accidents (RoSPA)'s Sir George Earle Trophy – the UK's premier award for occupational safety. Powergen's excellent performance in occupational health was also recognised by RoSPA with the award of a Commendation in the Astor Trophy.

Throughout 2000, the management of safety in the UK generation and CHP businesses continued to be extremely effective, while further advances were made in the retail business where the challenges include call centre safety management and the safety of sales staff out in the field. The distribution business also made significant progress towards achieving world class standards of safety performance. The acquisition of LG&E will provide further opportunities to share best practice across the Group.

Occupational health issues addressed during the year included the prevention of musculo-skeletal injuries and the effective management of work pressure. Powergen's welfare programme continued to offer significant support to both current and retired employees, with 17 per cent of employees making use of the PowerAssist employee assistance scheme during the year.

Community Powergen's UK programme of community involvement is focused on support for education, environmental action projects and projects to meet the needs of its local communities.

The Company completed the third year of its Weather Reports project, which has now benefited more than 900 primary schools and 27,000 children. The project is an exciting way for young people to learn about science, technology and mathematics.

Through the Powergen Environment Fund, the Company funded 13 local projects that achieve the objectives of local and national sustainability strategies and benefit local communities in which the Company has a presence.

During the year, Powergen agreed to support the development of the National Forest Millennium Discovery Centre in Leicestershire. The Centre is being created on 150 acres of reclaimed colliery land and will offer an interactive experience centred on the wide variety of life in a British woodland.

Powergen also repeated its campaign with Age Concern to provide free testing of electric blankets in areas surrounding the Company's sites. Powergen also continued its work with the charity NEA (National Energy Action) to fund long-term projects that ensure practical and detailed energy efficiency advice is made available to those communities that need it most.

Each year, the Company's employees vote for the national charity they would like to become the Company's charity of the year. Shelter was chosen as the charity of the year for 2000, and benefited from donations throughout the year as a result of Group activities linked to charity.

In the US, LG&E has a comprehensive programme to support charitable, educational and community-based projects throughout Kentucky. Powergen is committed to continuing this programme.

Financial review

Overview

This has been a year of significant change for Powergen, and this is reflected in the Group's financial position.

As part of the move to focus on the UK and US, and in order to reduce debt levels, we decided to sell a number of assets, both in the UK and overseas. This led in the UK to the disposal of Cottam power station, for £398 million, which completed on 31 December 2000, and an agreement to sell Rye House power station, for £220 million, which we expect will complete during March. Overseas, we have announced a number of disposals, which we expect to complete in the first half of 2001. Our Asia–Pacific interests, including development projects, will be sold to CLP International, and we will retain a 20 per cent stake in the companies. We have also announced the disposal of our interest in Tapada in Portugal. We expect the proceeds from the sale of these assets, and the associated reductions in debt, to total over £1,000 million.

2001 will see the completion of this disposal process which will leave the Group clearly positioned in the Anglo–American marketplace.

Group financial results

The results for the year to 31 December 2000 include, for the first time, trading from our US subsidiary, LG&E Energy Corp. (LG&E), which was acquired on 11 December 2000. From 2001 onwards, we expect the operations in the US to contribute significantly to the Group's operating profits.

Profit before tax, exceptional items and goodwill amortisation was £517 million, compared to £580 million for the same period last year. Earnings per share on the same basis was 66.7p, compared with 73.4p for the 12 months to 2 January 2000. After charging goodwill amortisation of £75 million, including £4 million in respect of LG&E, profit before tax and exceptional items was £442 million, compared with £512 million in the previous year.

Turnover

Group turnover grew by £445 million during the year to £4,191 million, an increase of almost 12 per cent. Turnover in the UK increased by £188 million, mainly within the wholesale and trading business due to additional sales of gas into the national transmission system and to third parties. In International Operations, turnover increased by £141 million, primarily due to the inclusion of a full year's sales from GPEC in India (GPEC became a subsidiary during July 1999). In addition, the commissioning of Csepel II in Hungary in November also contributed to the International sales figure. Turnover also included £116 million from our US Operations for the 21 days in December for which we owned LG&E.

Turnover is analysed at Figure 1 below:

Figure 1 Turnover

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m
UK Operations		
Electricity and gas – wholesale and trading	**1,893**	1,685
Electricity – distribution	**307**	376
Electricity and gas – retail	**1,726**	1,751
Cogeneration and renewables	**115**	95
Internal charges from distribution to retail	**(191)**	(245)
	3,850	3,662
US Operations	**116**	–
International Operations	**225**	84
	4,191	3,746

Operating Costs

Details of the Group's operating costs are set out in note 2 to the accounts. The pre-exceptional figures are summarised below. The 'acquisitions' column represents the operating costs of LG&E for the 21 day period of Powergen's ownership.

Figure 2

	Year ended 31 December 2000 Total £m	Year ended 31 December 2000 Continuing activities £m	Year ended 31 December 2000 Acquisitions £m	Year ended 2 January 2000 £m
Fuel costs	**707**	**678**	**29**	643
Pool purchases and other costs of sales	**2,202**	**2,156**	**46**	1,722
Staff costs	**213**	**203**	**10**	235
Depreciation, excluding exceptionals	**213**	**205**	**8**	263
Goodwill amortisation	**75**	**71**	**4**	68
Other operating charges, excluding exceptionals	**383**	**365**	**18**	366
	3,793	**3,678**	**115**	3,297

Fuel costs within the Group rose from £643 million to £707 million, including £29 million in the US. Excluding the LG&E figure, on a like for like basis, fuel costs increased by £35 million. This increase was the net result of two offsetting factors. In the UK, wholesale and trading business costs fell by £52 million, as generation reduced from 47.0TWh in 1999 to 43.2TWh in 2000. In the CHP business and in International Operations costs rose by £11 million and £80 million respectively, in line with increases in turnover in those businesses following the commissioning of new plant.

In the UK, pool purchases and other costs of sales continue to include: the cost of electricity purchased to meet customer sales obligations (pool purchases); charges from the National Grid Group and Regional Electricity Companies for the use of their transmission and distribution systems, and costs of the gas trading and retail businesses. In the US, they include power purchasing and related costs. These costs rose by £480 million compared with the previous year, due to increases in the number of retail customers and their related electricity purchase costs, an increase in gas trading activities, and the inclusion of £46 million of costs from LG&E.

Staff costs at £213 million were lower than in the previous year. Excluding the impact of US costs of £10 million, they fell by almost 14 per cent from £235 million to £203 million. This was due to a reduction in staff numbers, primarily in the UK distribution business. Staff numbers at 31 December 2000 totalled 11,742 of whom, 5,637 were in the UK, 5,343 in the US and 762 in International Operations.

The Group's depreciation charge for the year fell by £50 million compared with the previous 12 months. The 1999 results included £45 million of additional depreciation relating to the UK generation portfolio as we continue to review the appropriateness of the carrying value of assets held. In 2000, the comparable figure was only £1 million net.

Other operating charges include the costs of running the UK, US and International businesses, together with the supporting corporate infrastructure. Major business costs include maintenance and overhaul costs at power stations, business rates in the UK and insurance costs.

Operating income

Other operating income was £182 million this year compared with £191 million in the year to 2 January 2000. The 2000 figure included £99 million of deferred warranty income as part of the disposal arrangements for Fiddler's Ferry and Ferrybridge C power stations in July 1999 (1999 figures included £60 million in respect of this item), and £23 million of property income.

Other operating income also included £60 million of income from the asset disposal arrangement entered into with Eastern (now part of TXU Corp.) during 1996. In the year to 2 January 2000 this operating lease income totalled £84 million. The figure this year fell due to lower generation by Eastern, and the ending of certain earn-out arrangements in March 2000.

Exceptional items

The Group's results for 2000 include a number of one-off exceptional items, which are described in detail in note 3 to the accounts. These items fall into four categories: those associated with the disposal of assets in the UK and overseas; those associated with purchasing LG&E; costs associated with the valuation of our CHP plant portfolio in the UK and finance costs incurred as part of restructuring our long-term debt portfolio.

The disposal of assets include a profit of £337 million on the sale of Cottam power station in the UK on 31 December 2000 and a provision of £107 million for the write down of our Australian and Indian assets to value them in accordance with the sale agreement announced in early December. The sale of Australian assets completed on 27 February 2001. We also incurred £26 million of exceptional costs relating to the disposal of our International business, including staff severance costs.

One-off costs of purchasing LG&E include a number of severance and other payments to senior executives at the company and costs of raising the debt to finance the acquisition itself. Other financing costs reflected the buy-back of three long-term bonds acquired with our purchase of Powergen Energy in July 1998. This buy-back will facilitate the separation of our UK supply and distribution businesses as required under the Utilities Act.

The value of our generating plant across the Group is regularly reviewed in the light of changing market conditions. Recent increases in gas prices and falls in electricity sales prices mean that the carrying value of our CHP plant portfolio is impaired, and a write down in value of £79 million has therefore been made in these accounts.

Operating profits

Operating profits excluding exceptional items and goodwill amortisation totalled £728 million for the year compared with £791 million in the same period to 2 January 2000. Within UK Operations, profits fell by £119 million to £646 million. Wholesale and trading profits fell by £160 million. Lower wholesale prices were largely responsible for this fall, but the impact of these lower prices, coupled with the loss of generation volume following the sale of Ferrybridge C and Fiddler's Ferry power stations during 1999, could have caused an even larger fall in profits. However, as a result of our integrated trading strategy we were able to retain some additional value, including £21 million of LOLP as a result of strong plant availability.

The distribution business saw profits fall by £38 million to £116 million. This was the net result of a £44 million reduction from the P0 cut and £10 million of one-off metering costs, offset by £16 million of cost savings in the distribution business.

Within the retail business, profits increased by £39 million from £3 million to £42 million. Improvements in margins and increases in customer numbers, together with a reduction in IT project costs, more than offset increased marketing spend and the costs associated with signing up new customers.

CHP profits rose by £4 million to £18 million with the first contribution from the Winnington CHP scheme, the Group's largest scheme to date, which became fully operational in August 2000.

Results from International Operations totalled £121 million, compared with £79 million in the year to 2 January 2000. This year's figure included a significant contribution from GPEC in India which was consolidated as a subsidiary throughout 2000, but in which we only held a 27.8 per cent stake until July 1999. Development and administration costs fell with the winding down of development activities and the closure of overseas offices.

A more detailed analysis of operating profits is set out below, at Figure 3:

Figure 3 Operating Profits

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m
UK Operations		
Electricity and gas – wholesale and trading	**288**	448
Electricity – distribution	**116**	154
Electricity and gas – retail	**42**	3
Cogeneration and renewables	**18**	14
Lease and other income	**182**	146
	646	765
US Operations*	**8**	–
International Operations	**121**	79
Corporate costs	**(47)**	(53)
Operating profit before exceptional items and goodwill amortisation	**728**	791

* from 11 December 2000

Goodwill

Goodwill amortisation rose from £68 million in 1999 to £75 million in 2000. The increase was principally due to the acquisition of LG&E, which added £4 million to the charge during the year, and the additional stake in GPEC.

Interest costs

Pre-exceptional interest costs total £211 million for the year, in line with the previous 12 months' figure which was also £211 million. Within this figure, Group interest costs fell by £5 million, and interest costs in associates and joint ventures rose by £5 million. The Group interest charge included £5 million of interest costs within LG&E and £10 million of interest costs on the debt used to finance the purchase of LG&E. On a like for like basis therefore Group costs fell by £20 million, reflecting lower average levels of debt during most of 2000, compared with 1999. 2000 figures also included £81 million of exceptional interest costs (net of a £26 million foreign exchange gain) relating to the financing costs referred to within exceptional items above.

Inflation

In the view of the Company, inflation has had only a minimal impact on the Group's results from operations and financial position during the period under review.

Treasury management

As the Powergen Group has developed, treasury management has become more complex and diversified. In particular, the increase in debt in the Group's balance sheet as a result of the acquisition of LG&E in December 2000 has highlighted the importance of effective treasury management, and has increased Powergen's exposure to interest costs and the US Dollar/Sterling exchange rate.

Powergen has a central Group treasury department. It is responsible for treasury strategy, all funding requirements, the management of financial risks including interest rate and currency exposure, banking relationships, cash management and other treasury business throughout the Group. In addition, there are operational treasury teams in the UK and the US which service the treasury requirements of the UK and US businesses. Powergen's treasury activities are carried out in accordance with Board approved treasury policies, and all treasury operations comply with detailed treasury procedures which are approved at Board level. All treasury interfaces with banks and other third parties are governed by dealing mandates, facility letters and other agreements. Within treasury there is a segregation of front, middle and back office activities.

Treasury employs a continuous forecasting and monitoring process to ensure that the Group complies with all its banking and other financial covenants, and also the regulatory constraints that apply to the financing of the UK and US businesses.

Powergen does not enter into speculative treasury arrangements in that all transactions in financial instruments are matched to an underlying business requirement, such as planned purchases or forecast debt requirements. All treasury operations and planned activities are reported and discussed at a monthly treasury committee that is chaired by the Group Finance Director. Treasury activities are internally audited several times each year.

Treasury works in close liaison with the various businesses within the Group, when considering hedging requirements on behalf of their activities. A Group-wide cash forecasting and currency exposure reporting process exists which ensures regular reporting into treasury of future positions, both short and medium term.

Powergen takes steps to limit its credit exposure to banks and other counterparties. Exposure limits are set following credit analysis, and aggregate exposures are monitored on a Group-wide basis.

As part of its operating activities, Powergen engages in asset based energy marketing in the gas and electricity markets to assist in the commercial risk management and optimisation of both UK electricity and gas assets and to manage the price and volume risks associated with its UK retail business. The Group's portfolio is strictly monitored and controlled through delegated authorities and procedures, including transaction limits and credit risk management, which ensure that changing levels of exposure are appropriately managed. To achieve this portfolio optimisation Powergen uses fixed price bilateral contracts, futures and option contracts traded on commodity exchanges and swaps and options traded in over the counter financial markets.

There has been no change since the year end to the major financial risks faced by Powergen, or to its approach to the management of these risks. The year end position as described above is representative of the Group's current position in terms of its objectives, policies and strategies, which continue to evolve as the Group's business develops.

Foreign exchange risk management

During 2000, the majority of Powergen's income and expenditure was settled in Sterling. Following the acquisition of LG&E, a significant proportion of the enlarged Group's income and expenditure flows will be denominated in US Dollars. The Group also has some exposure to other foreign currencies including Euros and Australian dollars, but this exposure is likely to diminish with the disposal of the International business.

Powergen has Board approved policies dealing with transaction exposures (typically trading cash flows which impact the profit and loss account) and translation exposures (the value of liabilities and assets in the balance sheet). Powergen's policy is to hedge all contractually committed transaction exposures, as soon as the commitment arises. Powergen also covers a proportion of forecast foreign currency cash flows, and will also hedge more uncertain cash flows if this is appropriate, using flexible financial instruments that do not commit the Group. Anticipated US Dollar dividends from LG&E have been largely matched against expected US Dollar outflows.

Powergen's policy towards translation exposures is to hedge these exposures where practicable, with the intention of protecting the Sterling net asset value. These hedges are normally achieved through a combination of borrowing in local currency, forward currency contracts or foreign currency swaps. The value of the LG&E acquisition has been hedged in this way.

Where the foreign currency exposure is hedged, the value of the exposure is translated into Sterling at the exchange rate achieved in the associated hedging contracts. Details of the Group's foreign exchange contracts and swaps are set out in note 30 to the accounts.

Interest rate risk management

The Powergen Group has a significant portfolio of debt, and is exposed to movements in interest rates. This exposure is to both Sterling and US Dollar interest rates, although a limited exposure to interest rates of other currencies exists including Euros. Powergen manages these interest rate movements primarily through the use of a combination of fixed and floating rate borrowings and interest rate swaps. Powergen's policy is to target a ratio of fixed rate debt to floating rate debt of 50 per cent/50 per cent. However, this is managed within a 66 per cent/34 per cent and 34 per cent/66 per cent band, split between three debt portfolios (UK business, US business and US acquisition debt).

Group funding

Powergen's Board approved policy towards funding is to ensure that the Group is not constrained by lack of funds at any time, and not unreasonably or imprudently bound by restrictive covenants, or liquidity risks. Within this objective, the Group seeks to manage its cost of borrowing to minimise interest charges, while maintaining a stable, long-term funding base.

With the significant increase in the Group's debt position following the acquisition of LG&E, minimising the cost of borrowing has become a significant priority for the Group. The acquisition itself was funded from a combination of drawings under the US $4,000 million facility put in place for that purpose and cash held on short-term deposit. Some of this bank finance will be repaid with the proceeds of disposals referred to above. Since the acquisition, Powergen has commenced a refinancing strategy designed to reduce the overall cost of this debt. The first stage was the signing of a US $3,000 million commercial paper programme, under which Powergen has borrowed £33 million at 31 December 2000. Secondly, Powergen has securitised its UK retail trade debtors through a £300 million programme. Thirdly, since the year end, LG&E has also signed a US $125 million receivables securitisation programme. The interest rate payable for money borrowed under each of these programmes is lower than that for the acquisition facility.

The Group continues to manage its overall funding profile through a combination of committed bank term facilities, long-term capital market funding, and short-term uncommitted capital market and bank facilities. Further refinancing activity is anticipated during 2001.

At 31 December 2000, the Powergen Group had total borrowings of £5,931 million (2 January 2000 £2,670 million) including £3,628 million of long-term loans and £2,303 million of short-term loans and overdrafts.

The bank term loans referred to above contain financial covenants. In addition, the bank loans, all the bonds and the securitisation programmes contain other conditions with which Powergen must comply. There are also constraints and financial covenants imposed by various regulatory authorities. None of these covenants or conditions is considered onerous and treasury monitoring procedures are described above.

At 31 December 2000, the Group had £609 million of cash and short-term investments (2 January 2000 £646 million). Powergen's policy is to place any surplus funds on short-term deposit with approved banks and financial institutions. £442 million of this amount represented Sterling deposits. Strict limits governing the maximum exposure to these banks and financial institutions are applied. The majority of this cash was invested with AAA rated money funds.

The Group's net borrowing position at 31 December 2000 therefore was £5,322 million, compared to £2,024 million at 2 January 2000. The overall interest rate for the year, when compared to average net borrowings, was 6.7 per cent compared with 6.9 per cent in the previous year. Gearing (net debt as a percentage of net assets plus net debt) was 70 per cent at the end of the year, compared with 50.5 per cent at 2 January 2000.

Cash flow from operations

The consolidated cash flow statement on page 27 is prepared in accordance with FRS1(revised). Net cash flow can be summarised below, at Figure 4:

Figure 4

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m
Cash flow from operations	**847**	692
Gas contract re-negotiation payments	**–**	(719)
Operating cash flow	**847**	(27)
Interest	**(129)**	(154)
Exceptional interest	**(107)**	–
Tax	**10**	26
Dividends	**(227)**	(162)
Free cash flow	**394**	(317)
Capital expenditure and investment	**(306)**	(387)
Acquisition expenditure – LG&E	**(3,918)**	–
Acquisition expenditure – other	**(73)**	(434)
Sale of investments	**55**	203
Asset disposal proceeds	**398**	1,282
Other	**47**	33
Trading cash flow	**(3,403)**	380
Exchange movements	**99**	–
Issue of shares	**6**	4
Net cash flow	**(3,298)**	384

Cash flow from operations of £847 million was £155 million higher than in the previous year.

Interest payments fell to £129 million which reflected lower debt levels for most of the year. Powergen also paid £107 million of exceptional interest costs for the bond buy-backs and financing costs of the LG&E acquisition, as mentioned in exceptional items above.

The tax position shows a net receipt of £10 million. This consists of £27 million of tax payments across the Group, net of £37 million of refunds received from the Inland Revenue in the UK following the agreement of some prior year tax computations.

The dividend figure in 2000 represents the second interim dividend for 1999 and the interim payment for 2000. The previous year's figure was lower since it included the final dividend for 1998, which was only for a nine month period.

Free cash flow was £394 million. Excluding the one-off impact of gas contract payments in 1999, this was a similar free cash flow to the previous year. Capital expenditure and investment totalled £306 million, including £12 million of loan repayments from associated undertakings. It included £254 million within the UK, £27 million in the US and £25 million on other overseas projects. A full analysis of expenditure is set out at Figure 5.

The acquisition cost for LG&E included the payment of £2,229 million for shares, together with £24 million of capitalised acquisition costs. The total figure for acquisition costs will be £29 million, the remaining amount of £5 million will be paid in early 2001. The total amount of £3,918 million also includes the fair value of debt acquired with LG&E of £1,665 million.

Other acquisitions include £34 million for an additional 14 per cent stake in GPEC, £34 million for a 50 per cent stake in Corby Power Limited which joins the UK generation portfolio and £5 million for a 50 per cent stake in TeleCentric Solutions Limited, a joint venture to develop multi-billing capability and telecommunication skills in the UK retail business.

Asset disposal proceeds reflect the sale of Cottam power station in the UK for £398 million, which was completed on 31 December 2000.

In summary, excluding the purchase of LG&E, net cash flow for the year was positive at £620 million. After the purchase of LG&E net cash flow was negative at £3,298 million, and net debt rose by that amount during the year from £2,024 million at 2 January 2000 to £5,322 million at 31 December 2000.

Figure 5

Capital expenditure and investment	**Year ended 31 December 2000 £m**	Year ended 2 January 2000 £m
UK:		
Wholesale and trading	**25**	72
Distribution	**101**	72
Cogeneration and renewables	**97**	53
Retail	**5**	10
Cottam Development Centre	**–**	45
Others	**31**	45
Loan repayments	**(5)**	(12)
	254	285
US	**27**	–
International:		
Tapada do Outeiro	**–**	10
GPEC	**6**	–
Paiton II	**9**	8
Csepel II	**14**	82
LG Korea	**2**	28
Others	**1**	–
Loan repayments	**(7)**	(26)
	25	102
	306	387

In addition to the amounts shown above, at 31 December 2000 the Group had commitments of £108 million for capital expenditure and investment, of which £48 million relates to UK expenditure, £16 million to US expenditure and £44 million relates to international projects, principally Paiton.

Taxation

The tax charge, excluding exceptional items, amounts to £71 million for the year compared with £99 million for the same 12 months to 2 January 2000. This figure includes £5 million of tax credits relating to US Operations. The effective rate, before exceptional items and goodwill, is 13.7 per cent compared with 17.1 per cent in the year to 2 January 2000.

An exceptional tax credit of £44 million arises on the various exceptional items booked in these accounts. This comprises £3 million of tax charges on the Cottam disposal, £4 million of tax credits on disposing of International Operations, a £9 million tax credit on US acquisition and financing costs and £34 million of tax credits on the bond buy–backs. Tax credits on exceptional items in 1999 totalled £49 million.

Dividends

The second interim dividend to be paid on 30 March 2000 is 25.4p, giving a total dividend payment of 36.2p for the year. This represents a 4 per cent increase on the total figure paid in respect of 1999 of 34.8p. From the beginning of 2001 we will report our results and pay dividends on a quarterly basis. This move will benefit shareholders and lead to a smoothing of dividend payments over the four quarters.

US GAAP information

A reconciliation between the Group's results in accordance with UK GAAP and those results in accordance with US GAAP is set out on pages 47 to 49 of the accounts. The major movements this year result from the acquisition of LG&E. The principal differences are in respect of deferred tax, pensions and goodwill.

Board of Directors

as at 31 December 2000

Chairman and Chief Executive

Edmund Wallis (61). He was appointed on 22 October 1998, having been Chief Executive of PowerGen UK plc since March 1990 and Chairman since July 1996. He is a non-executive director of Mercury European Privatisation Trust plc and a non-executive director of London Transport.

He stood down as Chief Executive on 21 February 2001.

Directors

Paul Myners* (52) Deputy Chairman (non-executive). He is the senior independent director, and was appointed on 31 May 1999. He has been chairman of Gartmore Investment Management plc since 1987. He is also non-executive chairman of Guardian Media Group and is a member of the Financial Reporting Council. He was formerly an executive director of National Westminster Bank plc and a non-executive director of Celltech Group plc and Orange plc. He was a non-executive director of PowerGen UK plc between 1990 and 1996. He chairs the Remuneration and Nomination Committees.

Nick Baldwin (48) Executive director, UK Operations. He was appointed on 22 October 1998, having been a director of PowerGen UK plc since February 1998 and managing director, UK Electricity Production since 1996. He joined the CEGB, the predecessor of Powergen, in 1980 and his previous appointments with PowerGen include director of Generation, director of Strategy and Head of Strategic Planning. He is a non-executive director of Electricity Association Limited and a director and Trustee of Midlands Excellence.

He was appointed Chief Executive on 21 February 2001

Sir Frederick Crawford* (69) (non-executive). He was appointed on 22 October 1998, having been a non-executive director of PowerGen UK plc since June 1990. He is chairman of the Criminal Cases Review Commission and a Fellow of the Royal Academy of Engineering. He has held appointments as Professor of Electrical Engineering at Stanford University, and as Vice-Chancellor of Aston University for 16 years. He was formerly a non-executive director of Legal and General Group plc and Rexam plc.

Sydney Gillibrand CBE* (66) (non-executive). He was appointed on 31 May 1999. He is chairman of AMEC plc and TAG Aviation (UK) and a non-executive director of ICL, and Messier-Dowty. He was previously vice-chairman of British Aerospace plc. He is chairman of the Audit Committee.

Anthony Habgood* (54) (non-executive). He was appointed on 22 October 1998, having been a non-executive director of PowerGen UK plc since November 1993. He is Chairman of Bunzl Plc., having joined that company in 1991. He was previously chief executive of Tootal Group plc. He is a non-executive director of Schroder Ventures International Investment Trust plc

Mr Habgood stood down as a director of the Company on 31 January 2001. He ceased on that date to be a member of the Audit Committee.

Roger Hale (57) Executive director and director of LG&E Energy Corp. He was appointed a director on 11 December 2000 having been chairman and chief executive of LG&E Energy Corp. since August 1990. He is also a director of H&R Block, Inc.

Mr Hale will stand down as a director on 30 April 2001.

Peter Hickson (55) Group Finance Director (executive). He was appointed a director on 19 June 1998, having been Group Finance Director of PowerGen UK plc since July 1996. Prior to that, he was Group Finance Director of MAI plc from 1991 having previously held senior positions in Tarmac and United Scientific Holdings. He is a non-executive director of Lex Service plc.

Dr David K-P Li* (61) (non-executive). He was appointed a director on 22 October 1998, having been a non-executive director of PowerGen UK plc since January 1998. He is chairman and chief executive of The Bank of East Asia Limited, having been a director since 1977 and holds directorships of numerous companies in the Far East and elsewhere including The Hong Kong and China Gas Company Limited.

Roberto Quarta* (51) (non-executive). He was appointed a director on 22 October 1998, having been a non-executive director of PowerGen UK plc since July 1996. He is chief executive of BBA Group plc, having joined the board in 1993, and has also been a director of BTR plc.

Company Secretary

David Jackson (47) Company Secretary.

* Independent non-executive director.
All non-executive directors were members of the Audit, Nomination and Remuneration Committees until 17 November 2000. With effect from 17 November 2000, the members of the Audit and Remuneration Committees were as follows:

Audit Committee	Sydney Gillibrand CBE (Chairman)
	Sir Frederick Crawford
	Anthony Habgood
Remuneration Committee	Paul Myners (Chairman)
	Dr David Li
	Roberto Quarta

All non-executive directors continue as members of the Nomination Committee and Paul Myners continues as Chairman.

As part of a Group reorganisation effective from 9 December 1998, a new holding company, Powergen plc, was put in place. The previous quoted company named PowerGen plc changed its name to PowerGen UK plc.

Directors' report

The directors present their report and the audited accounts of Powergen plc for the year ended 31 December 2000.

Activities

The Company is the holding company of a Group whose principal activities are electricity production and distribution, and energy trading and retailing. Following the acquisition by the Company of LG&E Energy Corp. ('LG&E'), completed in December 2000, the Group's activities are located mainly in the UK and the mid-West region of the US with other residual international investments. The Chairman's Statement and the Operating and Financial Review, which form part of this report, describe the development of the business during the financial period and the outlook for the future. They also contain information about the Group's research and development activities and events which have taken place since 31 December 2000.

The Company is committed to ensuring that the environmental implications of its business in all of the countries in which it operates are properly identified, assessed and managed. The Company publishes Environmental Performance Reports on its activities. Copies of the 2000 Report will be available from the Company Secretary.

A Health and Safety Report is also published regularly, and the Company reports on community and other matters in the Annual Report and the Annual Review which is sent to shareholders.

From next year the Company intends to produce a Corporate Social Responsibility report covering a broader spread of its activities. A summary of the Company's engagement in this area is included in this year's Annual Review.

On 22 December 2000 the Secretary of State for Energy redeemed the Special Rights Redeemable Preference share in the Company held on behalf of the Government. Consequential amendments to the Articles of Association following from this will be proposed at the forthcoming Annual General Meeting.

Profit and dividends

Profit before taxation for the year ended 31 December 2000 (including the period following the completion of the acquisition of LG&E on 11 December) was £517 million before exceptional items and amortisation of goodwill (a decrease on the figure for the year to 2 January 2000 of £580 million).

The directors have declared a second interim dividend for the year of 25.4p net per ordinary share, payable on 30 March 2001 to shareholders on the record at 2 March 2001. Added to the first interim dividend paid on 3 November 2000, this makes a total dividend for the year of 36.2 p net per ordinary share, compared with a total dividend paid for the year ended 2 January 2000 of 34.8p net per ordinary share.

After providing for taxation (£27 million) and a minority interest (£12), and after payment of the dividend (£236 million), the retained profit for the year amounted to £193 million.

Substantial shareholdings

As at 1 March 2001, the Company had been notified of the following interests in three per cent or more of the issued ordinary share capital of the Company:

- Brandes Investment Partners L.P. (7.8 per cent);
- The Capital Group of Companies, Inc including its affiliates (7.77 per cent)
- Franklin Resources, Inc (7.025 per cent);
- The Bank of New York (6.249 per cent) underlying the ADRs;
- and CGNU plc and certain of its subsidiaries (3.49 per cent).

The Company is not aware of any other interest in the issued ordinary share capital of the Company of three per cent or more.

Property

The property clawback arrangements entered into at the time of the first public offers of shares in the generation and Regional Electricity companies which entitle HM Government to a proportion of any gains (above certain thresholds) accruing to the Group on certain property disposals expired on 31 March 2000.

Directors

For clarity of presentation, information required in accordance with the provisions of the Companies Acts regarding the remuneration, share options and beneficial interests of the directors and the interests of the directors and their families in the share capital of the Company is included in full in the Report on Directors' Remuneration and Related Matters starting on page 19, as are details of the service contracts, if any, of all the directors.

Employees

The Company provides an environment in which communication is open and constructive. There are well-established arrangements for communication and consultation with employees and their representatives at local and Group level covering a wide range of business and employment issues. The views of staff are both sought and taken into account, an Employee Opinion Survey being one way in which they are regularly measured.

Powergen is committed to offering equal opportunities to both current and prospective employees. The Company continues to review and develop best practices and procedures to ensure that all staff are treated fairly in all aspects of employment. It also strives for a diverse environment that is supportive of all staff. Individual differences which do not relate to job performance such as gender, marital status, sexual orientation, race, colour, ethnic origin, nationality, religion, age or disability are respected.

Powergen believes in ensuring that disabled people can compete fairly for job opportunities, training and development, through the promotion and development of best practices. Links and contacts with external disability networks and organisations are maintained to identify best practices and to provide work experience placements for disabled people. In the event of existing employees becoming disabled, Powergen will seek to maintain their employment through training, redeployment and adjustments to the job role and workplace, where it is reasonable and practicable to do so.

Training and development of staff remains a key priority in achieving Powergen's growth strategy and ensuring that all staff perform at the highest level. During 2000 two major business areas achieved Investors in People accreditation for the first time.

The Company encourages employee share ownership and operates a number of arrangements to encourage ongoing commitment to Powergen. These include three employee share schemes approved by the Inland Revenue for application in the UK: the Powergen ShareSave Scheme (1998), a share option scheme for employees; the Powergen Executive Share Option Scheme (1998), which is available for Powergen executives and senior management; and the Powergen 1998 Profit Sharing Scheme.

Contributions for political and charitable purposes
Donations to charitable organisations during the financial year by Powergen and its UK subsidiaries amounted to £247,523. Each year Powergen nominates a 'Charity of the Year' as the principal beneficiary for charitable activities. Shelter was the charity so designated in 2000 after consultation with staff.

No political donations were made.

Policy on payment of creditors
Where appropriate in relation to specific contracts, the Company's practice is to:

(a) settle the terms of payment with the supplier when agreeing the terms of each transaction;

(b) ensure that those suppliers are made aware of the terms of payment by inclusion of relevant terms in the contracts; and

(c) pay in accordance with its contractual and other legal obligations.

In the UK, the Company supports the Better Payments Practice Code, copies of which may be obtained from the Department of Trade and Industry, and has in place well developed arrangements with a view to ensuring that this is observed in all other cases. In the US and elsewhere overseas, Group companies are encouraged to adopt equivalent arrangements by applying local best practices.

The average number of days taken to pay the Company's trade suppliers calculated in accordance with the requirements of the Companies Act is 28 days.

Authority to purchase own shares
General authority was given on 5 June 2000 for the purchase by the Company of up to 10 per cent of the Company's existing issued share capital. This authority was still valid at the end of the year ended 31 December 2000, being due to expire at the end of the 2001 Annual General Meeting. The directors intended that this power would be exercised only under certain circumstances and it is proposed that the authority be renewed at the forthcoming Annual General Meeting.

Details of a Qualifying Employee Share Trust set up to acquire shares in the Company in the market are given in Note 25 to the Accounts.

Summary financial statements
The Company is permitted under the Companies Act to send its shareholders summary financial statements in place of its full Report and Accounts. Full financial statements are available to shareholders on request and will be provided on receipt of a written request to the Company Secretary to that effect.

Auditors
A resolution to reappoint the auditors, PricewaterhouseCoopers, and to authorise the directors to fix their remuneration will be proposed at the forthcoming Annual General Meeting.

Annual general meeting
The third Annual General Meeting of the Company will be held on Tuesday 1 May 2001 at 11:00 am at The ICC, Birmingham. A Circular letter from the Chairman of the Company explaining the business to be considered at the meeting, together with a Notice of the Meeting, accompanies this Report.

Euro
The Powergen Group recognises the wide implications of the Euro for businesses, including impacts on commercial arrangements and financial systems. Appropriate preparation is being made in those of its entities resident in countries already having adopted the Euro, based on the EU timetable for transition towards the introduction of hard currency in January 2002. Within the UK, the Group's preparations recognise the uncertain position regarding possible UK entry to the single currency as well as the needs of customers and suppliers. Continuing developments, including the possibility of a referendum on entry, are monitored closely.

Directors' responsibilities
Company law requires the directors to prepare accounts for each financial period which give a true and fair view of the state of affairs of the Company and of the Group and of the profit or loss of the Group for that period. The accounts have been prepared on a going concern basis and a statement confirming this is included in the Report on Corporate Governance beginning on page 17.

In preparing the accounts, the directors confirm that they have:

- selected suitable accounting policies and applied them consistently;
- made judgements and estimates that are reasonable and prudent; and
- followed applicable accounting standards.

The directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the accounts comply with the Companies Act 1985. They are responsible for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

A copy of the financial statements of the Company is placed on the Powergen plc website. The maintenance and integrity of the website is the responsibility of the directors and the work carried out by the auditors does not involve consideration of these matters. Accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board
D J Jackson
Company Secretary
2 March 2001

Report on Corporate Governance

The Board of Powergen is pleased to have the opportunity to report to shareholders on the manner in which it has applied the principles of good governance as set out in Section 1 of the Combined Code. As the standards of corporate governance have continued to be refined over time through the reports of the Cadbury, Greenbury and Hampel committees and the Turnbull Working Party, the Powergen Board has been active in ensuring that the Company's practice has remained in line with best practice.

In preparing this report, the Board has considered the manner in which it has applied the Principles of Good Governance ('Principles') and the extent to which it has complied with the Code of Best Practice ('Combined Code'). As described below, the roles of Chairman and Chief Executive have been combined during the year under report as a consequence of which the Company has not complied with Principle A.2 of the Combined Code. The roles have now been separated. In all other respects the Company has complied with the Combined Code throughout the year.

The Board of Directors

The Powergen Board has always had a balance of executive and non-executive directors with, in the latter years, a preponderance of independent non-executive directors. During the year under report, four executive and six non-executive directors have served on the Board. Mr Roger Hale was appointed as an executive director on 11 December on the completion of the Company's acquisition of LG&E Energy Corp. Since the end of the year, Mr Anthony Habgood stood down from the Board on 31 January 2001 and Mr Roger Hale will stand down on 30 April 2001. The Company has announced that Mr Vic Staffieri will be appointed an executive director on 30 April 2001. Brief personal details of each of the directors serving at the end of the year are given on page 14. All of the non-executive directors regularly attend meetings of the Board and its committees and play a full part in the deliberations of matters reserved to the Board.

All of the non-executive directors are considered to be independent in accordance with principle A.3.2 of the Combined Code. All directors are required to submit themselves for re-election at regular intervals, at least every three years.

The Board acknowledges that the principles of good governance indicate that there should be a clear division of responsibilities between the running of the Board and executive responsibility for the running of the Company's business. In 1996, Mr Ed Wallis was appointed to act as Chairman and Chief Executive of the Company. Mr Paul Myners, a non-executive director appointed in 1999, holds the position of deputy chairman and is the senior independent director on the Board. Mr Wallis continued to act in the combined role during the year.

The Board has always kept this position under regular review and has previously indicated that proposals for the separation of the roles will be brought forward at the appropriate time. On 21 February 2001 the Board announced that Mr Wallis was standing down as chief executive with Mr Nick Baldwin assuming that role with immediate effect. Mr Wallis continues as Chairman.

The Board has reserved to itself powers in respect of areas significant to the Group's business including the approval of the corporate plans and annual budgets; acquisitions and disposals of segments of the business; major investment and financial decisions; appointments to the Board and to the Boards of subsidiary companies, and changes to the management and control structure within the Powergen Group, including key policies and procedures and delegated authority limits.

The Board meets routinely at regular intervals with additional meetings taking place as necessary. All directors are fully briefed in advance of Board meetings on the matters to be discussed and have access to any further information they may require. The Board has considered annually the strategy and direction of the Group at an extended meeting over a two-day period. In total the Board met ten times in the last year. To facilitate the smooth transaction of business within the Company, the Board has established a number of standing and adhoc committees. The terms of reference of each committee have been approved by the Board and, where applicable, comply with the recommendations of the Combined Code.

The Board has three standing committees, the Remuneration Committee, the Audit Committee and the Nomination Committee. The Remuneration and Audit Committees were both established in 1990.

Procedures are in place to facilitate access to independent outside advice for directors.

Remuneration Committee

The composition and activities of the Remuneration Committee are described in a separate report on pages 19 to 23.

Audit Committee

During the year under report, until 17 November 2000 the Audit Committee comprised all the non-executive directors. With effect from 17 November 2000 members of the Audit Committee were Mr Sydney Gillibrand CBE (as chairman), Sir Frederick Crawford and Mr Anthony Habgood. All executive directors have a right to attend meetings of the Committee. The Committee has written terms of reference and its activities are described below on page 18. The Committee met twice during the year. All meetings are attended by senior members of the Company's external auditors and the head of the Company's internal audit department. The Audit Committee reviews issues of accounting policy and presentation for external financial reporting and monitors the work of the internal audit function. It also ensures an objective and professional relationship is maintained with the external auditors, including reviewing the fees paid by the Company in respect of non-Audit services. The Committee has full access to the auditors both internally and externally who, in turn, have access at all times to the chairman of the committee, Mr Sydney Gillibrand CBE.

Nomination Committee

The Nomination Committee was set up in 1992. All non-executive directors are members under the chairmanship of Mr Paul Myners. The Committee meets as and when required. It has met once in the last year. The Nomination Committee provides a formal and transparent procedure for appointments of new directors to the Board.

Directors' remuneration

The Board has since 1996 set out its policy on directors' remuneration in detail in the Annual Report. The Board's present policies, together with the detailed description of the packages of individual directors can be found in the report on the Directors' Remuneration and Related Matters. The Remuneration Committee keeps under regular review the development of good practice in the structuring and terms of executive directors' remuneration packages. The policy of the Committee remains one of ensuring that the high quality management that is required by the Company's developing businesses both in the UK and abroad is recruited and retained. The achievement of business goals and individual personal development are key areas upon which the Committee focuses its attention. The Committee ensures that a strong link is maintained between the level of remuneration and individual performance against agreed targets. The Company's arrangements are such that no director is involved in deciding his or her own remuneration.

The Committee have considered the compensation commitments of executive directors' service contracts should they be terminated early and have taken a robust line by reducing compensation to reflect departing directors' obligations to mitigate loss. The Committee acknowledges that there may be advantages in providing explicitly in the initial contract for compensation commitments to be fixed and will give active consideration to implementation in future contracts.

Relations with shareholders

Since its creation, the Company has, through its Investor Relations and Company Secretary's Departments, maintained an active dialogue with its shareholders both small and large presently totalling some 700,000 individual accounts. The very fact of being a 'privatisation stock' with an initial register exceeding 1.5 million has meant that shareholder communication has always been high on the Company's agenda. The Investor Relations Department, reporting to the Group Finance Director, has an active programme of contact with institutions and brokers which involves not only presentations at the time of the announcement of the Company's preliminary and interim results but also visits to the Company's facilities and briefings by operational management on particular parts of the Company's business. These briefings have included visits to the Company's overseas assets and businesses, including LG&E Energy Corp. The Company publishes documentation used at the time of these briefings through the internet.

The Company has for some years now used the Annual General Meeting as a means of communicating with private investors by treating the event as more than just a business meeting. This is particularly so now that the Company has some three million customers in the UK, a significant proportion of whom are also shareholders. The meeting includes a presentation on the Company's activities following which shareholders are invited to ask questions. Private investors have shown considerable interest in the Company through attendance both at the Annual General Meeting and also at Extraordinary General Meetings. The Chairmen of the three standing Committees regularly attend the Annual General Meeting.

The Company has at its meetings indicated the level of proxies lodged on each resolution by disclosure of the percentage of shares voting.

Reporting and Internal Controls

Good corporate governance is of prime importance for the Company in demonstrating to all of those who have an interest in the Company's affairs, that it is acting in accordance with, and, where possible, exceeding best practice. The Company's reputation is of significant value and adherence to the principles of corporate governance is one of the prime methods by which that reputation is supported.

Throughout 2000, the Board has operated procedures meeting the requirements of the Combined Code relating to internal control as set out in the September 1999 guidance 'Internal Control Guidance for Directors on the Combined Code' from the Turnbull Committee. Given that practice in this area continues to evolve, the Board and the Audit Committee continue to keep under review the manner in which the Company reports its position and prospects.

The directors recognise their responsibility for reviewing the effectiveness of the system of internal control. A system of internal control is designed to ensure that the risks facing the business in pursuit of its objectives are identified and managed at known and acceptable levels. It is the case, however, that as with any such system, controls can only provide reasonable and not absolute assurance against material misstatement or loss.

During 2000, and the period prior to signature of the published accounts on 2 March 2001, the Board has continued its ongoing process of identifying, evaluating and managing the key commercial and financial risks facing the business together with more general risks, such as those relating to compliance with laws and regulations. This evaluation of risks has led to the development of specific management strategies to address issues involved in the achievement of its business objectives whilst complying with the regulatory regimes in the countries within which the Group operates.

LG&E was acquired on 11 December 2000, just three weeks before the year end. Action was taken during the acquisition process to ensure that key risk areas had been identified and that suitable control arrangements were in place for LG&E as it became part of the Powergen Group.

The Board has maintained clear lines of accountability and documented delegations of authority which set out the proposed actions which need to be referred to the Board for its prior approval. These delegations are subject to periodic review as to their implementation and their continuing suitability within the evolving business and have been further reviewed as part of the integration of LG&E into the business of the Company.

Group Policies are in place for key issues including the management of Health and Safety, Environmental, Engineering and IT risks, as well as defining the Board's requirements for personal conduct and probity. Corporate values, which emphasise team working and ethical behaviour, have been fully communicated to staff. Again, these issues have been reviewed as part of the LG&E acquisition.

The manager of each business unit has clear accountabilities for ensuring appropriate control procedures are in place.

The Board and its committees receive specific regular reports from management on key risk areas and senior managers confirm annually that they have complied with a number of the Group Policies. The Board's evaluation includes a specific assessment of long- and short-term risks and opportunities identified by each of the business units as part of the Group's annual planning process. This ensures that local objectives are set in the context of the Group's overall corporate vision, strategies and objectives.

This plan underpins the approved budgets. The Board has reviewed the Group's budget and cash flow forecasts for the year ended 31 December 2001 and the outline projections for the four subsequent years. The directors confirm they have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, the directors continue to adopt the going concern basis in preparing the Company's consolidated statements.

Performance of the Group is reviewed monthly by executive directors and by the Board. Reports to the executive directors and to the Board include variance analysis and projected forecasts for the year compared to the approved budgets and non-financial performance indicators, cash management, covenant compliance and progress with significant initiatives and projects.

The Board has continued its practice of undertaking a specific review of the effectiveness of the Group's system of internal controls as operated during the year ended 31 December 2000. This has included a review of the process adopted throughout the Group whereby business units and responsible directors have assessed local arrangements.

The Group's Internal Audit Department conducts reviews which include the control of financial systems and their associated computer environments, business unit operations, and compliance with policies, particularly relating to health and safety, regulation and the environment. Reports, including where relevant action plans agreed with local management, are circulated to responsible senior managers and directors and are reviewed by the Audit Committee.

The monitoring arrangements in place give reasonable assurance that the structure of controls and their operation is appropriate to the Company's and Group's situation.

Report of the Board on Directors' remuneration and related matters

The Board of Powergen is pleased to report on the policy for the remuneration of directors and other matters relating to the benefits and interests of directors. Responsibility for the determination of the remuneration packages of executive directors lies with the Remuneration Committee. The remuneration of non-executive directors is a matter for the Board as a whole.

The Remuneration Committee

Membership of the Remuneration Committee was reviewed during the year. Until 17 November, the Committee comprised all the non-executive directors under the chairmanship of Mr Paul Myners. Since that date, the members have been Dr David Li, Mr Roberto Quarta and Mr Paul Myners who continues to serve as Chairman. The Committee met three times during the year. The Chairman of the Board, Mr Ed Wallis, attends meetings of the Committee other than when matters concerning himself are under discussion. The Committee is responsible for developing remuneration policy, determining the remuneration packages of the executive directors, administering the Company's incentive schemes for employees (including the grant of share options) and ensuring that the Company has a developed succession policy and that such policy is kept under review.

In establishing a package of remuneration and other benefits applicable to the executive directors and other senior employees and in reviewing the level of payments involved, the Committee has given full consideration to the Combined Code.

The members of the Committee receive fees as set out on page 20 and no other benefits.

Remuneration policy

In constructing the remuneration package ('package') for executive directors, the goal of the Committee is to provide for salary at the median level with the opportunity for upper quartile reward through the payment of bonuses where exceptional performance so warrants.

The Committee has established a strong link between the level of remuneration and performance against agreed targets. By so doing, it is the aim of the Board that financial performance can be achieved and business goals met. A clear focus on performance also assists the Company in developing individuals to attain their full potential.

The package comprises a number of separate elements which include base salary, bonus arrangements (both annual and medium term), retirement and certain non-cash benefits. The package aims specifically to align the interests of executives with those of the Company's shareholders.

In reviewing the individual elements of the package, the Committee has taken advice from independent consultants, principally from Hay Group, and considered external surveys and packages within comparable companies. The Committee wishes to ensure that increases in salaries and benefits reflect the performance of the Company and of the individual executives when measured against practice and performance in comparable companies.

The bonus arrangements and share option schemes outlined below are performance based and performance targets are agreed by the Committee. Performance is measured against profit and other targets set from the Company's annual budget and plans and from the returns provided to shareholders. Financial targets agreed annually by the Board as part of the planning and budgeting review process are reviewed by the Committee to ensure that they are appropriate yardsticks for judging the performance of the Company and of individuals. Executive directors and senior employees are encouraged to take incentive payments in the form of shares and to retain the holding of those shares.

The Committee keeps the package in its entirety under review. During the year, with the assistance of external consultants, the Committee considered the composition of the packages of the directors. Following this, the Committee decided, in April 2000, to make an enhanced grant of share options, subject to performance criteria, to incentivise directors and senior employees. As a result, no grants were made under the Medium Term Bonus Scheme to executive directors. Separately, the means by which Total Shareholder Return, one of the main performance measures, is assessed were reviewed and brought into line with best practice. Advice was also taken on the implications of the acquisition of a substantial US subsidiary. A review of the issues involved has been commissioned and is continuing.

Other than as outlined above, no change in the package has taken place during the year under report.

The Committee is aware of the requirements of the Utilities Act relating to the application in certain cases of performance criteria related to service standards and intends to reflect these as the relevant provisions come into effect.

Details of the compensation package and information on each individual director are given below. On 11 December the Company purchased LG&E Energy Corp. The compensation arrangements for that company are described separately below. Copies of directors' employment contracts and agreements, together with documentation supporting the various schemes described, are available for inspection by shareholders at the Company's registered office.

Summary of Directors' Emoluments

	Year ended 31 December 2000					Year ended ended 2 January 2000				
	Salaries/ fees £000	Benefits £000	Performance related bonuses £000	Other payments £000	Total £000	Salaries/ fees £000	Total £000	**Total accrued pension p.a. at 31 December 2000 £000**	Pension p.a. accruing in year ended 31 December 2000 £000	Transfer value of Increases, at 31 December 2000 £000
Chairman										
Edmund Wallis	503	33	220	27	783	470	897	347	13	224
Executive directors										
Nick Baldwin	285	12	140		437	245	413	143	24	304
Roger Hale*	32	7	545		584			501		
Peter Hickson**	295	11	192		498	283	455	44	10	173
Non-executive directors										
Sir Frederick Crawford	25	–	–	–	25	23	23			
Sydney Gillibrand CBE	30	–	–	–	30	18	18			
Anthony Habgood	25	–	–	–	25	23	23			
Dr David Li	25	–	–	–	25	28	28			
Paul Myners	55	–	–	–	55	32	32			
Roberto Quarta	25	–	–	1	26	23	23			

*The figures for Roger Hale relate to the period from 11 December 2000, the date of his appointment.
In addition to the above emoluments, Roger Hale received payments of £9,538,464 to which he became entitled as a director of LG&E under change of control arrangements in his contract with LG&E, and as a shareholder of LG&E.
**Peter Hickson also received 1,989 additional matching shares under the terms of the Annual Bonus Scheme.

Note:
The pension information shown above are accrued benefit entitlements and transfer values of relevant increases in accrued benefits calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. The amounts represent the total accrued pensions payable at normal retirement date of age 60, the increase or decrease in that amount during the year and the transfer value of relevant increases in accrued benefit during the year.

Performance-related bonuses have been calculated as the aggregate value of:
(i) payments earned during the year, except where payment is deferred and the amount of the payment remains dependent on future performance and/or subject to forfeiture; plus
(ii) payments earned in previous years which have ceased to be dependent on future performance and/or forfeiture during the year

Where payment arises in the form of shares, the value attributed to the shares has been calculated based on the market price of the shares either at the time the shares were awarded or, if later, the time the award ceased to be dependent on future performance and/or subject to forfeiture. Increases in value of share awards resulting from the addition of the share equivalent of dividends during deferral periods are included in executive directors' emoluments only up to the time the award ceased to be dependent on future performance and/or subject to forfeiture.

Options over ordinary shares granted to, and exercised by, the executive directors

	Options held at 3 January 2000			Options granted during year			Held at 31 December 2000	First date of exercise	Expiry date
Name	Date Granted	Price	Number	Date	Price	Number			
Edmund Wallis	01.12.92	£2.78	25,500				25,500	01.12.95	01.12.02
	01.07.93	£3.87	27,500				27,500	01.07.96	01.07.03
	22.11.94	£5.57	53,500				53,500	22.11.99	22.11.04
	29.11.95	£5.32	56,000				56,000	29.11.00	29.11.05
	26.06.96	£5.32	63,500				63,500	26.06.01	26.06.06
	02.07.97	£7.35	20,000				20,000	02.07.02	02.07.07
	25.09.98	£8.88	50,500				50,500	25.09.03	25.09.08
	12.03.99	£8.70	10,500				10,500	12.03.04	12.03.09
				10.04.00	£3.995	364,000	364,000	10.04.03	10.04.10
			307,000				**671,000**		
(ShareSave)				05.04.00	£2.95	3,283	3,283	01.06.03	30.11.03
							3,283		
Nick Baldwin	22.11.94	£5.57	11,000				11,000	22.11.97	22.11.04
	29.11.95	£5.32	13,000				13,000	29.11.98	29.11.05
	26.06.96	£4.705	15,500				15,500	26.06.99	26.06.06
	02.07.97	£7.35	14,000				14,000	02.07.00	02.07.07
	25.09.98	£8.88	20,500				20,500	25.09.03	25.09.08
	12.03.99	£6.875	32,500				32,500	12.03.04	12.03.09
				10.04.00	£3.995	195,000	195,000	10.04.03	10.04.10
			106,500				**301,500**		
(ShareSave)	24.07.96	£3.77	4,575				**4,575**	01.08.01	31.01.02
							4,575		

Options over ordinary shares granted to, and exercised by, the executive directors – continued

Name	Date Granted	Price	Options held at 3 January 2000 Number	Options granted during year Date	Price	Number	Held at 31 December 2000	First date of exercise	Expiry date
Roger Hale*				11.12.00	$35.13	74,864	**74,864**	immediate	03.02.09
Peter Hickson	11.12.96	£5.72	78,500				78,500	11.12.01	11.12.06
	02.07.97	£7.35	32,000				32,000	02.07.02	02.07.07
	25.09.98	£8.88	30,500				30,500	25.09.03	25.09.08
	12.03.99	£6.875	21,000				21,000	12.03.04	12.03.09
				10.04.00	£3.995	217,000	217,000	10.04.03	10.04.10
			162,000				**379,000**		
(ShareSave)	25.07.97	£5.81	1,678				1,678	01.08.00	31.01.01
(ShareSave)				01.06.00	£2.95	3,283	3,283	01.06.03	30.11.03
							3,283		

* Roger Hale was appointed a director on 11 December 2000 on completion of the acquisition of LG&E. The options were granted under rollover arrangement applicable to all holders of LG&E shares under the terms of the Merger Agreement relating to the acquisition. The options relate to American Depositary Receipts, each representing four Powergen shares.

Options granted on or after 22 November 1994 are subject to performance criteria.

Details of options exercised and lapsed during the year under the Medium Term Bonus Scheme are given on page 22. No options were exercised by the executive directors during the year. The following options lapsed during the year:

Number	Value	Date granted	Date lapsed	
Peter Hickson	1,678	£5.81	25.07.97 (Sharesave)	04.04.00

The mid-market price for ordinary shares in Powergen plc on 31 December 2000 was 632p. The price range during the period 2 January 2000 to 31 December 2000 was 328.25p (low) to 635p (high).

Notice Period of Employment Contracts

During the year under report, Mr E A Wallis had a service contract with the Company with entitlement to a rolling two-year period of notice originally entered into on 31 March 1991. Mr P C F Hickson and Mr N P Baldwin each has a service contract with the Company which can be terminated on a rolling one year period of notice. Mr P C F Hickson first entered into his contract on 9 July 1996 and Mr N P Baldwin first entered into his on 24 February 1994. It is the policy of the Committee that the Company should not enter into contracts with rolling notice periods exceeding one year for any executive director to be appointed in future.

On 21 February 2001 Mr E A Wallis' contract was amended to a fixed term expiring on 22 February 2003 and in other respects to reflect his new role specifically as Chairman of the Board; in particular to reduce his salary with effect from February 2002 to £200,000 p.a. as his involvement in the affairs of the Company reduces to two days a week and to limit any payment due on the termination of his contract by the Company to a maximum of the salary capable of being earned in the period from 1 March 2001 to the expiration of the contract less any salary or bonus paid to him in the period between 1 March 2001 and the date of such termination.

If the contract of either of Mr P C F Hickson or Mr N P Baldwin is terminated by the Company other than in the circumstances described below, the benefits for which the Company is liable will be not more than a termination payment of up to full salary and benefits for the outstanding period of the contract and benefits and enhanced early retirement under the Company's pension schemes, subject to mitigation by the individual concerned.

On 23 October 1998 Mr P C F Hickson and Mr N P Baldwin each entered into a Deed of Amendment of their service contract to provide for a termination payment of twice gross annual salary plus target annual bonuses and compensation for pension benefits to be made in certain circumstances where their employment is terminated either by the Company or by themselves following a change control in the Company (which payments are not subject to mitigation by the individual concerned). A change in control means the acquisition of the Company by a third party or a merger of the Company with an undertaking of comparable size. On 21 February 2001, Mr E A Wallis' contract was amended to limit any payment to him under an equivalent provision to that set out above.

Mr R W Hale joined the Board of Powergen on 11 December 2000. He has a three year fixed term contract which expires on 10 December 2003. It has been the practice of the Board to appoint directors with contracts initially of fixed term of greater than one year which reduce to a rolling one year period. The Board considered that the term of Mr Hale's contract, although greater than one year, was desirable to facilitate his recruitment to the Board and retention within Powergen following the acquisition of LG&E. Mr Hale has given notice of his retirement on 30 April 2001 when he will step down from the Board. Under the terms of his contract, he will be entitled to retirement benefits as described below on page 23. He will receive no other severance benefits.

Annual Bonus Schemes

UK

Payments under the scheme are dependent, in all cases except Mr E A Wallis, on the achievement of corporate and personal performance targets. Mr E A Wallis' annual bonus is determined solely according to corporate performance.

Corporate performance is measured against the level of the Company's earnings per share excluding any exceptional items. The payment of a bonus is conditional upon achievement of a defined level of earnings per share. A level of bonus of 25% of base salary is achieved for on-target performance increasing on a straight line basis to a maximum of 40% for exceptional achievement. The amount of any bonus for executive directors is determined by the Committee. In the light of the substantial challenges for the business and accomplishments during the year under report, the Committee determined to include in the Annual Bonus award certain ex-gratia sums. Bonuses awarded for the year 2000 are set out on page 20.

Annual bonus payments may be made in either cash or shares. To encourage executive directors to take bonuses in shares, shares issued in lieu of bonus payments may be put into trust. Subject to an individual director holding such shares for three years and remaining an employee of Powergen, additional matching shares on the basis of one for four will be issued by the Company to him in respect of the shares at the end of that period.

During the year, Mr P C F Hickson called for the transfer to him of 7,956 shares issued under this scheme, together with 1,392 shares representing dividends accrued. He also received matching shares as shown on page 20.

US

Mr R W Hale is a member of the Short Term Incentive Plan offered by LG&E to certain of its directors and senior managers. The Plan provides for cash awards on the basis of both company and individual performance. In Mr Hale's case, company performance is based on annual increase in earnings per share before exceptional items achieved by Powergen and profit before tax for LG&E. The target level of bonus for Mr. Hale for 2001 is anticipated to be set at 70% of annual salary, increasing up to a maximum of 122.5% for exceptional performance.

Medium Term Bonus Scheme

This scheme is based on the performance of the Company over a five-year period and was first introduced in the 1994/95 financial year. Membership of the scheme is limited to executive directors selected at the discretion of the Committee. Mr E A Wallis, Mr P C F Hickson and Mr N P Baldwin are currently members. As indicated above, there was no award of shares under this scheme in 2000. The numbers of shares placed in trust under the scheme are:

	At 2 January 2000	Lapses during Year Date		Exercises during Year Date		At 31 January 2000
Edmund Wallis	124,891	24.05.00	21,277	18.04.00	19,097	84,517
Peter Hickson	57,809					57,809
Nicholas Baldwin	22,632					22,632

David Dance, a former director, retains an entitlement to 4,453 shares under the scheme. The performance criteria relating to their exercise were waived when he left the Company. During the year he exercised his entitlement to 11,216 shares under the scheme, including shares representing accrued dividends.

Performance targets relate to Total Shareholder Return, the performance of the Company being measured against that of a comparator group of the FTSE 100 companies at the date a grant is awarded. Awards under the scheme are in the form of restricted shares which are held by Trustees (the Powergen Employee Share Trust), shares equivalent to the value of the annual bonus of a participating executive director for the previous year (currently 40 per cent of salary) being placed in Trust. For the shares to vest, and the director to be able to call for the transfer of shares to him, the Company must meet the target criteria over a period of three to five years. Half of the shares first become eligible to vest on the third anniversary of the grant, but the actual number of shares available for transfer to the director depends on the Company's performance against the comparator group over the intervening period. No shares are released if the Company is in the lower half of the comparator group and a maximum of 100 per cent are released if the Company is in the top quartile. Subject to continuing performance from the date of initial grant, all outstanding shares become eligible to vest successively on the fourth and fifth anniversaries of the grant, after which the award is lost if target performance has not been achieved.

No shares placed in trust under the scheme have vested during the year. On 18 April 2000, Mr E A Wallis exercised options under the scheme over 19,097 shares granted in June 1994 and which had previously vested. He received in addition 892 shares representing dividends accrued since the date of the award. On 24May 2000, the grant of options over 21,277 shares made to Mr Wallis on 24 May 1995 lapsed under the terms of the scheme. Executive directors (and former directors) first became eligible to call for the transfer of the vested shares under the scheme on 7June 1998.

In the event of the employment of an individual by Powergen being terminated in certain specific circumstances not including resignation or of the take-over of the Company the performance criteria attached to grants under the scheme are waived and all outstanding options may be exercised.

The scheme does not apply to LG&E.

Share options

UK

The Powergen Executive Share Option Scheme was originally established in 1991 and was approved by shareholders and the Inland Revenue. The Rules of the Scheme were amended by the Board in May 1996 under powers granted to them by the Scheme, to give effect to implications for the operation of the Scheme of the provisions of the Finance Act 1996. Membership of the Scheme is at the discretion of the Committee. Following the implementation of the Scheme of Arrangement in December 1998 the Scheme was replicated in respect of shares in the Company as the new holding company of the Group. All executive directors are members of the Scheme together with certain other senior executives and managers. Details of grants of options are given on pages 20 and 21; at all times these have been made in accordance with best practice as it has developed.

Grants of options are conditional upon the same specific performance criteria as those applicable to the Medium Term Bonus Scheme having been met at the time of exercise. The performance criteria are waived under the same circumstances as apply to the Medium Term Bonus Scheme. Options are exercisable between three and ten years after the date of grant (between five and ten years in the case of executive directors who are in receipt in the same year of a grant under the Medium Term Bonus Scheme). At the time when an option holder wishes to exercise his options, the performance of the Company in terms of Total Shareholder Return is compared with that of the relevant comparator companies.

Options are granted at the market price of the Company's shares at the time of grant. In normal circumstances, the maximum levels of grant calculated on the basis of the exercise price and the number of options for any one year for executive directors will be equivalent to their salary for that year; the maximum levels for other participants will be a proportion of their base salary. The issue of share options by the Remuneration Committee as described above during the year was in line with the ABI Guidance then in force and in some cases is in excess of four times salary.

US

Under Long-Term Incentive Plan schemes offered by LG&E to certain of its officers and senior managers, including Mr R W Hale, awards of share options as well as performance units (payable in cash and shares) may be made, the latter to vest subject to achievement of pre-determined company financial targets over a specified period (usually three years). The total value of an award will be determined as a percentage of base salary, ranging from 35 per cent for certain officers up to 175 per cent for Mr Hale for full achievement of targets.

Awards of both share options and performance units under the scheme are granted at the market price of Powergen American

Depository Shares ('ADS') as of the date of grant. Share options are subject to a one-year vesting requirement and, once vested, are exercisable at any time over a nine-year period.

Mr Hale's outstanding entitlements under his Long-Term Incentive Plan may be adjusted in the event of certain changes in the share capital structure of Powergen. In the event of a change of control of Powergen, all his stock options will immediately vest, and all performance-based awards be paid out in cash.

Retirement benefits

Mr E A Wallis, Mr P C F Hickson and Mr N P Baldwin are members of the Electricity Supply Pension Scheme (ESPS) and of the Powergen Senior Executive Pension Scheme. Members are entitled on normal retirement to a pension of two thirds of final year's base salary after twenty years' service, together with dependants' pensions in the event of death, a lump sum on death in service and a pension in the event of early retirement on the grounds of ill health. Contributions to the ESPS paid by the Company are determined by the actuary and are expressed as a percentage of total pensionable salaries. Members are required to contribute six per cent of their pensionable salary. In a similar way, the Company meets all the costs of the Powergen Senior Executive Pension Scheme which is also determined by an actuary and expressed as a percentage of pensionable salaries for all members. Further details of the ESPS are set out in note 22 on page 39.

Mr R W Hale is a participant in LG&E's Retirement Income Plan ('RIP') and a Supplemental Executive Retirement Plan ('SERP') as defined in his service contract. The RIP is funded by LG&E contributions pursuant to qualified plan requirements of US tax statutes. The SERP is an unfunded plan and is a contractual obligation of LG&E. The RIP provides for a retirement benefit expressed as a percentage, calculated on the basis of length of service, of final 36 months' salary including payments under the Short Term Incentive Plan but excluding payments under the Long Term Incentive Plan. In the event of his retirement on 30 April 2001, the SERP will provide for an annual retirement benefit to Mr Hale equivalent to 50% of his base salary and payment under the Annual Bonus Scheme based upon target performance applicable at the date of his retirement. Details of the LG&E pension Plans are set out in note 22 on page 39.

Powergen ShareSave Scheme

The Powergen ShareSave Scheme is an Inland Revenue approved Scheme available to all eligible employees. Non-executive directors are not eligible for membership. Following the implementation of the Scheme of Arrangement in December 1998 existing options held under the ShareSave Scheme were transferred to apply to shares in the Company, as the new holding company of the Group.

Options granted to executive directors under the Powergen ShareSave Scheme are included in the table on pages 20 and 21.

Other Benefits

Each executive director and certain other senior employees receive a car provided by the Company together with petrol for private mileage. Certain executive directors also have the use of a pool car and chauffeur and Mr R W Hale has the use of a plane to which the Company has "time share" access. Telephone rental charges are reimbursed and a mobile telephone is provided. The Company operates a private health insurance scheme through PPP.

Mr R W Hale also receives benefits in the provision of life insurance and in respect of business and personal club memberships and financial planning services.

Non-executive directors' remuneration

The remuneration of the non-executive directors is determined by the Board. The fees of non-executive directors consist of a basic sum plus an additional payment for specific duties in respect of the Deputy Chairman and the Chairmen of each of the three standing committees. There has been no increase in the fees during the year under report. Non-executive directors do not receive pension contributions and do not have service contracts with the Company or any of its subsidiaries. Each appointment of a non-executive director is subject to review on the third anniversary of the appointment.

Appointment of Directors

Mr V A Staffieri is to be appointed a director with effect from 30 April 2001. In accordance with the Company's Articles of Association, he will retire at the forthcoming Annual General Meeting and will offer himself for re-appointment.

Mr N P Baldwin and Dr David K-P Li will retire by rotation at the forthcoming Annual General Meeting and will offer themselves for re-appointment.

As at the date of the Annual General Meeting, there will be an unexpired term of one year on Mr N P Baldwin's service contract as his contract is subject to termination on one year's notice on a rolling basis. As at the date of the Annual General Meeting, there will be an unexpired term of 19 months on Mr V A Staffieri's service contract . Mr Staffieri has a fixed term contract of two years with the Company expiring on 10 December 2002 but subject thereafter to automatic one year extensions unless terminated upon 90 days prior notice. Mr Staffieri's contract was entered into on 11 December 2000 as part of the LG&E acquisition, before he was to be appointed a director. Dr David K-P Li is a member of the Remuneration Committee and he does not have a service contract with the Company or any of its subsidiaries.

Beneficial Interests

The beneficial interests of the directors in the ordinary share capital of Powergen plc are as follows:

	As at 31 December 2000	As at 2 January 2000
Nicholas Baldwin	4,866	4,379
Sir Frederick Crawford	7,398	7,398
Sydney Gillibrand CBE	6,858	6,858
Anthony Habgood	3,000	3,000
Roger Hale	–	–*
Peter Hickson	28,551	17,057
Dr David Li	20,000	20,000
Paul Myners	25,000	9,867
Roberto Quarta	3,000	3,000
Edmund Wallis	63,478	41,686

*The figure for Roger Hale is as at the date of his appointment, 11 December 2000.

There have been no changes in the beneficial interests of the directors in the ordinary share capital of Powergen plc between 31 December 2000 and the date of this Report.

In addition, certain Executive Directors have interests in shares held in the Powergen Employee Share Trust as shown on page 22.

There were no non-beneficial interests of the directors in the ordinary share capital of the Company.

No director had at any time during the period under report any interest (other than as a nominee on behalf of the Company) in the shares of any subsidiary company.

No director during the period under report had a material interest in any contract significant to the Group's business.

Report of the Auditors
to the members of Powergen plc

We have audited the financial statements which comprise the profit and loss account, the balance sheet, the cash flow statement, the statement of total recognised gains and losses and the related notes.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards issued by the Auditing Practices Board and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the United Kingdom Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report, the chairman's statement, the operating and financial review and the corporate governance statement.

We review whether the corporate governance statement reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Company's or the Group's corporate governance procedures or its risk and internal control procedures.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the United Kingdom Auditing Practices Board and with auditing standards generally accepted in the United States of America. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

United Kingdom opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group at 31 December 2000 and of the results and cash flows of the Group for the year then ended and have been properly prepared in accordance with the United Kingdom Companies Act 1985.

United States opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Group at 31 December 2000 and 2 January 2000 and the results of their operations and their cash flows for the year ended 31 December 2000, the year ended 2 January 2000, and the nine month period ended 3 January 1999, in conformity with accounting principles generally accepted in the United Kingdom. These principles differ in certain respects from accounting principles generally accepted in the United States. The effect of the differences in the determination of net income, shareholders' equity and cash flows is shown in the Summary of differences between UK and US generally accepted accounting principles.

PricewaterhouseCoopers
Chartered Accountants and Registered Auditors
London
2 March 2001

Consolidated Profit and Loss Account

for the year ended 31 December 2000

	Note	Year ended 31 December 2000 Before exceptional items £m	Year ended 31 December 2000 Exceptional items (note 3) £m	Year ended 31 December 2000 Total £m	Year ended 2 January 2000 Before exceptional items £m	Year ended 2 January 2000 Exceptional items (note 3) £m	Year ended 2 January 2000 Total £m	Nine months ended 3 January 1999 Total £m
Turnover		**4,485**	–	**4,485**	3,989	–	3,989	2,489
Group's share of associates' and joint ventures' turnover		**(294)**	–	**(294)**	(243)	–	(243)	(145)
Group turnover	1	**4,191**	–	**4,191**	3,746	–	3,746	2,344
– continuing activities		**4,075**	–	**4,075**	3,746	–	3,746	2,344
– acquisitions		**116**	–	**116**	–	–	–	–
Operating costs	2,3	**(3,793)**	**(97)**	**(3,890)**	(3,297)	(293)	(3,590)	(2,597)
Other operating income	2	**182**	–	**182**	191	–	191	100
Group operating profit/(loss)	2	**580**	**(97)**	**483**	640	(293)	347	(153)
– continuing activities		**579**	**(79)**	**500**	640	(293)	347	(153)
– acquisitions		**1**	**(18)**	**(17)**	–	–	–	–
Group's share of associates' and joint ventures' operating profit		**73**	–	**73**	83	–	83	44
Profit on disposal of fixed assets	3	–	**337**	**337**	–	543	543	(2)
Provision for loss on sale	3	–	**(133)**	**(133)**	–	–	–	–
Net interest payable								
– Group	5	**(151)**	**(81)**	**(232)**	(156)	–	(156)	(104)
– Associates and joint ventures		**(60)**	–	**(60)**	(55)	–	(55)	(30)
Profit/(Loss) on ordinary activities before taxation	6	**442**	**26**	**468**	512	250	762	(245)
Tax on profit on ordinary activities	7	**(71)**	**44**	**(27)**	(99)	49	(50)	89
Profit/(Loss) on ordinary activities after taxation		**371**	**70**	**441**	413	299	712	(156)
Minority interest		**(12)**	–	**(12)**	(4)	–	(4)	–
Profit/(Loss) attributable to shareholders		**359**	**70**	**429**	409	299	708	(156)
Dividends	8			**(236)**			(226)	(157)
Retained profit/(loss) for the year				**193**			482	(313)
Earnings/(Loss) per ordinary share	10			**65.9p**			109.0p	(24.1)p
Earnings per ordinary share (excluding goodwill amortisation and exceptional items)	10			**66.7p**			73.4p	38.8p
Diluted earnings/(loss) per ordinary share	10			**65.3p**			108.5p	(24.1)p
Dividends per ordinary share	8			**36.2p**			34.8p	24.1p

Statement of Total Recognised Gains and Losses

for the year ended 31 December 2000

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Profit/(Loss) attributable to shareholders	**429**	708	(156)
Revaluation reserve arising on acquisition	–	25	–
Currency translation differences on foreign currency net investments	**(32)**	63	(28)
Total recognised gains/(losses) for the year	**397**	796	(184)
Prior year adjustment	–	–	96
Total recognised gains/(losses)	**397**	796	(88)

The notes on pages 31 to 46 form part of these financial statements.

Balance Sheets
as at 31 December 2000

	Note	The Group 31 December 2000 £m	The Group 2 January 2000 £m	The Company 31 December 2000 £m	The Company 2 January 2000 £m
Fixed assets					
Goodwill	12	**2,627**	1,309	–	–
Tangible fixed assets	13	**5,964**	3,232	–	–
Investments	14	**600**	470	**3,100**	325
		9,191	5,011	**3,100**	325
Current assets					
Stocks	15	**258**	127	–	–
Debtors: amounts falling due after more than one year	16	**125**	11	–	–
Debtors: amounts falling due within one year		**1,061**	722	**181**	161
Less: securitisation of trade debtors		**(152)**	–	–	–
Net debtors falling due within one year	17	**909**	722	**181**	161
Cash and short-term deposits		**609**	646	–	–
		1,901	1,506	**181**	161
Creditors: amounts falling due within one year					
Loans and overdrafts	18	**(2,303)**	(98)	–	–
Trade and other creditors	19	**(1,574)**	(1,106)	**(166)**	(156)
Net current (liabilities)/assets		**(1,976)**	302	**15**	5
Total assets less current liabilities		**7,215**	5,313	**3,115**	330
Creditors: amounts falling due after more than one year					
Long-term loans	20	**(3,628)**	(2,572)	–	–
Other creditors	21	**(477)**	(415)	–	–
Provisions for liabilities and charges	23	**(731)**	(295)	–	–
Deferred tax	24	**(93)**	(47)	–	–
Net assets		**2,286**	1,984	**3,115**	330
Capital and reserves					
Called-up share capital	25	**326**	325	**326**	325
Share premium account	26	**9**	4	**9**	4
Other reserves	26	**656**	656	–	–
Revaluation reserve	26	**23**	25	–	–
Profit and loss account	26	**1,072**	909	**2,780**	1
Shareholders' funds (including non-equity shareholders' funds)		**2,086**	1,919	**3,115**	330
Minority interests (including non-equity)	27	**200**	65	–	–
		2,286	1,984	**3,115**	330

Approved by the Board on 2 March 2001

E A Wallis **P C F Hickson**

The notes on pages 31 to 46 form part of these financial statements

Consolidated Cash Flow Statement
for the year ended 31 December 2000

	Note	**Year ended 31 December 2000 £m**	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Cash flow from operating activities	29a	**847**	(27)	456
Dividends from associated undertakings		**2**	1	–
Returns on investments and servicing of finance				
Interest received		**59**	56	7
Exceptional interest paid		**(107)**	–	–
Interest paid		**(188)**	(210)	(83)
		(236)	(154)	(76)
Taxation		**10**	26	(176)
Capital expenditure and financial investment				
Purchase of tangible fixed assets		**(286)**	(329)	(175)
Purchase of fixed asset investments		**(32)**	(53)	(39)
Repayment of/(New) loans to associated undertakings		**12**	(5)	(4)
Sale of fixed asset investments		**55**	203	11
Sale of tangible fixed assets		**39**	18	53
Net receipts from disposal of power stations		**398**	1,282	–
		186	1,116	(154)
Acquisitions and disposals				
Purchase of subsidiary undertakings		**(2,253)**	(261)	(866)
Net cash acquired with subsidiary undertakings		**13**	–	1
Purchase of associates and joint ventures		**(39)**	–	–
Purchase of increased stake in subsidiary undertakings		**(34)**	–	–
Receipts from sale of subsidiary undertakings		–	5	253
Net cash disposed with subsidiary undertakings		–	–	(29)
		(2,313)	(256)	(641)
Equity dividends paid		**(227)**	(162)	(172)
Net cash (outflow)/inflow before use of liquid resources		**(1,731)**	544	(763)
Management of liquid resources				
Cash withdrawn from/(paid for) short-term deposits		**146**	(493)	31
Financing				
Issue of ordinary share capital		**6**	4	6
Debt due within one year:				
Use of US Dollar term facility		**1,173**	–	–
Use of Sterling term facility		**535**	–	–
Issue of commercial paper		**34**	–	–
Other movement in short-term loans		**(345)**	(76)	76
Debt due beyond one year:				
Redemption of bonds		**(427)**	–	–
Repayment of term loans		–	–	(200)
Use of US Dollar term facility		**1,038**	–	–
Movement in Sterling term facility		**(300)**	(600)	895
Issue of Eurobonds		–	570	–
Movement in Sterling equivalent long-term loans		**14**	41	(38)
		1,728	(61)	739
Increase/(Decrease) in cash in the year	29b	**143**	(10)	7

The notes on pages 31 to 46 form part of these financial statements

Principal Accounting Policies

Nature of operations
The Powergen Group has three main businesses; UK Operations, US Operations and International Operations. Powergen's principal business in the UK is the generation, distribution and sale of electricity and the sale of gas. Powergen's principal business in the US is the generation of electricity and the transmission, distribution and sale of electricity and gas. Powergen's principal business overseas, other than in the US, is the generation of electricity and associated energy-related businesses.

Basis of preparation of accounts
The financial statements are prepared under the historical cost convention and in accordance with applicable UK accounting standards. There is no difference between the profit on ordinary activities before taxation and the retained profit for the year stated on the face of the consolidated profit and loss account and their historical cost equivalents. Values of assets and liabilities vested in the Company on 31 March 1990 under the Transfer Scheme made pursuant to the Electricity Act 1989 are based on their historical cost to the Central Electricity Generating Board (CEGB).

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting year. Actual results can differ from those estimates.

In the accounts for the period ended 3 January 1999, figures for the three years ended 29 March 1998 were restated, following the adoption of Financial Reporting Standard 12, from 30 March 1998. This necessitated adjustment to provisions made in prior periods principally relating to major overhaul and decommissioning of generation plant.

On 9 December 1998, under a Scheme of Arrangement between the Company and its Shareholders, a new holding company was created for the Powergen Group, Powergen 1998 PLC (then renamed Powergen plc). A simultaneous capital reorganisation of Powergen UK plc (formerly Powergen plc) was accounted for as a Group reconstruction and merger accounting principles were applied.

Basis of consolidation
The consolidated accounts include the financial statements of the Company and all of its subsidiary undertakings, together with the Group's share of the results and net assets of associated undertakings and joint ventures. The results of subsidiaries sold or acquired are included in the consolidated profit and loss account up to, or from, the date on which control passes. All of the results of operations included in 'acquisitions' are continuing activities. Intra-group sales and profits are eliminated on consolidation.

Associated undertakings and joint ventures
The Group's share of profits less losses of associated undertakings and joint ventures is included in the consolidated profit and loss account. These amounts are taken from the latest audited financial statements of the relevant undertakings, except where the accounting reference date of the undertaking is not coterminous with the parent company, where management accounts are used. The accounting reference dates of associated undertakings and joint ventures are set out in note 14. Where the accounting policies of associated undertakings and joint ventures do not conform to those of the Group, adjustments are made on consolidation where the amounts involved are material to the Group.

Turnover
Turnover within the United Kingdom comprises sales of electricity, including fees under contracts for differences (Cfds), revenue from the sale of electricity and gas to industrial, commercial and domestic customers, and the sale of electricity and steam under combined heat and power schemes. The cost or the income attributable to Cfds is recorded when settlement is made. Where physical delivery under the Cfd has taken place prior to the year end, adjustment is made to account for the known variances between the contract strike price and the Pool price on the date of delivery.

Income from the sale of electricity and gas to industrial, commercial and domestic customers in both the United Kingdom and the United States is recognised when earned and reflects the value of units supplied, including an estimated value of units supplied to customers between the date of their last meter reading and the year end.

In the United States the amount of regulated income received from sales of electricity and gas to customers is determined by the Kentucky Public Services Commission. Under a three year rates order issued on 7 January 2000, Louisville Gas and Electric Company (LGEC) and Kentucky Utilities Company (KU) will operate under an earnings sharing mechanism until 31 December 2002. With regard to electricity income under this mechanism, incremental annual earnings for each utility resulting in a rate of return either above or below a range of 10.5 per cent to 12.5 per cent will be shared between shareholders and customers in the ratio 60:40.

Restructuring costs
Amounts are set aside for the Group's restructuring programme that involves the reorganisation or future closure of power station and other sites and specific reductions in staff numbers, where the Group is demonstrably committed to such actions.

Depreciation
Provision for depreciation of generating and other assets is made so as to write off, on a straight-line basis, the book value of tangible fixed assets. Assets are depreciated over their estimated useful lives or, in the case of leased assets, over the lease term if shorter. No depreciation is provided on freehold land or assets in the course of construction.

The estimated useful lives for the other principal categories of fixed assets are:

Asset	Life in years
Generating assets	20–60
Distribution and transmission networks	30–65
Other assets	3–40

Overhaul of generation plant
Overhaul costs are capitalised as part of generating assets and depreciated on a straight-line basis over their estimated useful life, typically the period until the next major overhaul. That period is usually between four and seven years.

Decommissioning
A fixed asset and related provision is recognised in respect of the

estimated total discounted cost of decommissioning generating assets. The resulting fixed asset is depreciated on a straight-line basis, and the discount on the provision is amortised, over the useful life of the associated power stations.

Foreign exchange

Assets and liabilities expressed in foreign currencies, including those of subsidiaries, associated undertakings and joint ventures, are translated to Sterling at the rate of exchange ruling at the end of the financial year. The results of foreign subsidiaries, associated and joint venture undertakings are translated to Sterling using average exchange rates.

Transactions denominated in foreign currencies are translated to Sterling at the exchange rate ruling on the date payment takes place unless related or matching forward foreign exchange contracts have been entered into when the rate specified in the contract is used. Differences on exchange arising from the re-translation of the opening net investment in and results of subsidiaries, associated undertakings and joint ventures are taken to reserves and, where the net investments are hedged, are matched with differences arising on the translation of related foreign currency borrowings. Any differences arising are reported in the statement of total recognised gains and losses. All other foreign exchange differences are taken to the profit and loss account in the year in which they arise.

Deferred income

Amounts received in advance in respect of the provision of services under warranty arrangements are taken to deferred income and recognised in operating income over the period to which the warranty cover relates. Costs associated with the provision of services under the warranty arrangements are netted against the operating income recognised, when incurred.

Financial instruments

The Group uses a range of derivative instruments including interest rate swaps, energy based futures contracts and foreign exchange contracts and swaps. Derivative instruments are used for hedging purposes, apart from energy based futures contracts, which are used for trading purposes. Interest differentials on derivative instruments are charged to the profit and loss account as interest costs in the period to which they relate. Accounting for foreign currency transactions is described in the foreign exchange policy set out above. Changes in the market value of futures trading contracts are reflected in the profit and loss account in the period in which the change occurs.

Debt instruments

Following the issue of Financial Reporting Standard 4 'Capital Instruments' all borrowings are initially stated at the fair value of consideration received after deduction of issue costs. The issue costs and interest payable on bonds are charged to the profit and loss account at a constant rate over the life of the bond. Any premium or discount arising on the early repayment of borrowings is written off to the profit and loss account as incurred.

Interest rate swaps

Interest rate swap agreements are used to manage interest rate exposures and are accounted for using hedge accounting. Amounts payable or receivable in respect of these agreements are recognised as adjustments to interest expense over the period of the contracts. The cash flows from interest rate swaps and gains and losses arising on terminations of interest rate swaps are recognised as returns on investments and servicing of finance.

Forward currency contracts

The Group enters into forward currency contracts for the purchase and/or sale of foreign currencies in order to hedge its exposure to fluctuations in currency rates. Unrealised gains and losses on currency contracts are not accounted for until the maturity of the contract. The cash flows from forward purchase currency contracts are classified in a manner consistent with the underlying nature of the hedged transaction.

Currency swaps

Currency swap agreements are used to manage foreign currency exposures and are accounted for using hedge accounting. In order to qualify for hedge accounting the instrument must be identified to a specific foreign currency asset or liability and must be an effective hedge. Foreign currency loans, where the repayment of principal is hedged by currency swaps, are included in the balance sheet at the Sterling equivalent of the hedged rate.

Goodwill

Goodwill arising on consolidation represents the excess or shortfall of the fair value of the consideration given compared to the fair value of the identifiable assets and liabilities acquired. Purchased goodwill is capitalised in the balance sheet and amortised on a straight-line basis over its estimated minimum useful economic life.

Negative goodwill is recognised in the profit and loss account on a straight-line basis over the life of the related fixed assets. Prior to the adoption of Financial Reporting Standard 10 'Goodwill and Intangible Assets' from 30 March 1998, goodwill arising was written off on acquisition against retained earnings. On disposal of trading entities, the goodwill previously written off to reserves is charged to the profit and loss account and matched by an equal credit to reserves. Goodwill arising on overseas acquisitions is regarded as a currency asset and is re-translated at each period end at the closing rate of exchange.

Tangible fixed assets

Tangible fixed assets are stated at original cost, net of customer contributions, less accumulated depreciation and any provision for impairment. Impairment losses are recognised in the period in which they are identified. In the case of assets constructed by the Company and its subsidiaries, directly related overheads and commissioning costs are included in cost.

Major assets in the course of construction are included in tangible fixed assets on the basis of expenditure incurred at the balance sheet date. Where borrowings are specifically financing the construction of a major capital project with a long period of development, interest payable, not exceeding the actual amount incurred during the relevant period of construction, is capitalised as part of the cost of the asset and written off over the operational life of the asset.

Operating leases

Rents payable under operating leases are charged to the profit and loss account evenly over the term of the lease. Income from operating leases is included within other operating income in the profit and loss account. Income is recognised on a straight-line basis except where income receipts vary with output or other factors. Any variable element is recognised as earned.

Fixed asset investments

The Group's share of the net assets of associated undertakings and joint ventures is included in the consolidated balance sheet. Other fixed assets investments are stated at cost less any provision for impairment in value. Investments in subsidiary undertakings are stated in the balance sheet of the parent company at cost, less any provision for impairment in value.

Fuel stocks and stores

Fuel stocks and general and engineering stores are stated at the lower of cost and net realisable value. In general, stocks are recognised in the profit and loss account on a weighted average cost basis. The Companies Act 1985 requires stocks to be categorised between raw materials, work in progress and finished goods. Fuel stocks and stores are raw materials under this definition.

US regulatory assets and liabilities

Statement of Financial Accounting Standard 71 'Accounting for the Effects of Certain Types of Regulation' (SFAS 71) sets out the appropriate accounting treatment for US utilities whose regulators have the power to approve or regulate charges to customers. As long as, through the regulatory process, the utility is substantially assured of recovering its allowable costs from, or is obligated to refund amounts to, customers, any costs/revenues not yet recovered, or refunded, may be deferred as regulatory assets/liabilities. Due to the different regulatory environment, no equivalent policy applies in the United Kingdom.

Under UK generally accepted accounting principles (GAAP), Powergen's policy is to recognise regulatory assets/liabilities established in accordance with SFAS 71 only where they comprise rights or other access to future economic benefits which have arisen as a result of past transactions or events which have created an obligation to transfer economic benefits to a third party. Measurement of the past transaction or event and therefore the amount of the regulatory asset/liability, is determined in accordance with UK GAAP.

Cash and short-term deposits

Short-term deposits include cash at bank and in hand, and certificates of tax deposit.

Deferred taxation

Deferred taxation arises in respect of items where there is a timing difference between their treatment for accounting purposes and their treatment for taxation purposes. Provision for deferred taxation, using the liability method, is made to the extent that it is probable that a liability or asset will crystallise in the foreseeable future.

Pensions and post-retirement benefits

The Group provides pension benefits through both defined benefit and defined contribution schemes. Pension costs are charged to the profit and loss account so as to spread the cost of pensions over employees' remaining working lives. The regular cost, and any variation from regular cost which is identified as a result of actuarial valuations, is amortised over the average expected remaining service lives of members. Differences between the amounts funded and the amounts charged to the profit and loss account are treated as either creditors or debtors in the balance sheet. Payments to defined contribution schemes are charged against profits as incurred.

Certain additional post-retirement benefits, principally health care benefits, are provided to eligible retirees within the Group's US Operations. The estimated cost of providing such benefits is charged against profits on a systematic basis over the average expected service lives of employees.

Notes to the Accounts

for the year ended 31 December 2000

1 Turnover

Turnover is analysed as follows:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
UK Operations			
Electricity and gas – wholesale and trading	**1,893**	1,685	1,155
Electricity – distribution	**307**	376	157
Electricity and gas – retail	**1,726**	1,751	1,001
Cogeneration and renewables	**115**	95	54
Other energy and hydrocarbon sales	–	–	89
Internal charges from distribution to retail	**(191)**	(245)	(119)
	3,850	3,662	2,337
US Operations*	**116**	–	–
International Operations	**225**	84	7
	4,191	3,746	2,344

* from 11 December 2000

Turnover analysed by geographic destination is not materially different from the analysis shown above.

Wholesale electricity trades in England and Wales are conducted according to a multilateral agreement between the electricity generators and the wholesale electricity purchasers. This multilateral agreement specifies the charges on each purchaser and the payments to each generator and ensures that the total charges equal the total payments. All such payments and charges are settled through a daily clearing account (the Pool) without passing through the ownership of a third party. Therefore although the customers of a specific generator are identified collectively as the purchasers who have signed the multilateral agreement, it is not possible to quantify the actual sales from one specific generator to one specific purchaser.

2 Operating profit

Operating costs were as follows:

	Year ended 31 December 2000 Total £m	Year ended 31 December 2000 Continuing activities £m	Year ended 31 December 2000 Acquisitions* £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Fuel costs	**707**	**678**	**29**	840	1,102
– burnt in power stations	**707**	**678**	**29**	643	567
– gas buy-outs	–	–	–	197	535
Pool purchases and other costs of sales	**2,202**	**2,156**	**46**	1,722	940
Staff costs (note 4)	**213**	**203**	**10**	235	139
Depreciation, including exceptional charges	**292**	**284**	**8**	263	157
Goodwill amortisation	**75**	**71**	**4**	68	28
Other operating charges, including restructuring costs	**401**	**365**	**36**	462	231
Operating costs, after exceptional items	**3,890**	**3,757**	**133**	3,590	2,597
Operating costs, before exceptional items	**3,793**	**3,678**	**115**	3,297	2,062
Exceptional depreciation charge (note 3)	**79**	**79**	–	–	–
Exceptional operating charges (note 3)	**18**	–	**18**	293	535

* US operations from 11 December 2000

The directors believe that the nature of the Group's business is such that the analysis of operating costs set out in the Companies Act 1985 format is not appropriate. As required by the Act, the directors have therefore adopted the presented format so that operating costs are disclosed in a manner appropriate to the Group's principal activities.

The depreciation charge for the year ended 31 December 2000 includes a net £1 million charge as the result of an impairment review of the Group's UK power station portfolio. This comprises a £21 million charge for an impairment in the current year and a £20 million credit for the reversal of an impairment recognised in a previous period (year ended 2 January 2000 £45 million charge, nine months ended 3 January 1999 £nil). The cash flows used in this impairment review were discounted at Powergen's cost of capital for UK Operations.

Other than foreign exchange gains disclosed in note 3, £14 million of foreign exchange losses were recognised in the profit and loss account.

Operating costs also include:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Repairs and maintenance costs	**88**	99	72
Research and development costs	**4**	5	5
Operating leases	**11**	6	17
(Profit)/Loss on disposal of fixed assets	**(21)**	1	(33)
Auditors' remuneration for audit of which £0.6 million paid to PricewaterhouseCoopers in the year ended 31 December 2000. In previous periods all audit fees were payable to PricewaterhouseCoopers	**0.7**	0.5	0.4
Auditors' remuneration for Company £nil in all periods			
Auditors' remuneration for non-audit services (of which £0.8 million paid to Coopers & Lybrand in the nine months ended 3 January 1999)	**2.6**	4.7	4.9

Fees for non-audit services comprise due diligence, accounting advisory, tax advisory services and other general consultancy, and include £1.7 million (£1.4 million in year ended 31 December 2000) in respect of the acquisition of LG&E Energy Corp. (LG&E) capitalised as part of the cost of acquisition (see note 11).

Other operating income includes £60 million (year ended 2 January 2000 £84 million, nine months ended 3 January 1999 £68 million) of income from operating leases. It also includes the recognition of £99 million (year ended 2 January 2000 £60 million) of deferred income in respect of the provision of services under warranty arrangements associated with the disposal of Fiddler's Ferry and Ferrybridge C power stations to Edison Mission Energy during 1999 (see note 3). This figure represents £100 million of deferred income recognised less £1 million of associated costs incurred during the period.

3 Exceptional items

Exceptional items comprise:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Asset impairment – UK Operations	**(79)**	–	–
US acquisition related costs	**(18)**	–	–
Re-negotiation of gas contract portfolio	–	(197)	(535)
Reorganisation and restructuring costs	–	(96)	–
Charged against operating profit	**(97)**	(293)	(535)
Bond buy-backs	**(66)**	–	–
US financing costs	**(15)**	–	–
Charged against interest costs	**(81)**	–	–
Profit on disposal of fixed assets – UK Operations	**337**	543	(2)
Asset impairment	**(107)**	–	–
Closure costs	**(26)**	–	–
Provision for loss on sale – International Operations	**(133)**	–	–
	26	250	(537)

Charged against operating profit

An impairment provision of £79 million has been made in respect of the Group's CHP plant portfolio in the light of changes in wholesale electricity and gas prices. The cash flows used in this impairment review were discounted at Powergen's cost of capital for CHP Operations.

As a consequence of the acquisition of LG&E, the Group has incurred costs totalling £18 million reflecting agreed payments to certain senior executives of LG&E.

On 19 October 1999, the Group agreed to pay £197 million to Liverpool Bay owners BHP Petroleum, LASMO and Monument Oil and Gas in exchange for modifications to their existing long-term gas supply contracts to Connah's Quay power station. This amount was paid in November 1999. During the nine months ended 3 January 1999, the Group agreed to pay £535 million to the same parties for amendments to their existing long-term gas supply contracts. This amount was also settled during 1999.

Reorganisation, restructuring and closure costs in UK Operations during 1999 represented the costs of restructuring and integrating the UK business consequent upon the acquisition of Powergen Energy in July 1998. The amount included committed severance payments and reorganisation costs.

In the year ended 31 December 2000, tax credits on the exceptional items charged against operating profits totalled £5 million (year ended 2 January 2000 £89 million, nine months ended 3 January 1999 £158 million).

Charged against interest costs

On 28 December 2000, Powergen repaid three Sterling Eurobonds originally issued by East Midlands Electricity plc (now Powergen Energy plc). The repayment of these bonds will facilitate the financial separation of its distribution and supply business, as required by the Utilities Act, which will come into force during 2001. The consideration paid to bond holders and the unwinding of hedging costs totalled £493 million. At 28 December 2000 the carrying value of these bonds was £427 million, giving a premium payable to buy out the bonds of £66 million.

During the year Powergen incurred arrangement and commitment fees totalling £28 million in respect of the $4,000 million term and revolving credit facility put in place to finance the acquisition of LG&E. Powergen also entered into an interest rate swaption arrangement to cap the interest rate payable under this facility at a cost of £13 million. As part of the financing arrangements for the acquisition, in early December, the Group entered into certain US Dollar denominated loan arrangements, which, on the acquisition date, crystallised foreign exchange gains totalling £26 million. These items, with a net cost of £15 million, have been included within exceptional US financing costs in these accounts.

In the year ended 31 December 2000, tax credits on the exceptional amounts charged against interest costs totalled £38 million (year ended 2 January 2000 £nil, nine months ended 3 January 1999 £nil).

Profit on disposal of fixed assets – UK Operations

On 31 December 2000, Powergen completed the sale of Cottam power station to Societe C2, a subsidiary company of London Electricity Group plc, for £398 million in cash. At the same time Powergen entered into arrangements to supply coal to the station for a 27 month period on terms consistent with Powergen's overall coal commitments.

Net assets disposed of, together with disposal costs, totalled £61 million, giving rise to an exceptional profit on disposal of £337 million. A £3 million tax charge arises on this disposal.

On 19 July 1999, Powergen completed the sale of Fiddler's Ferry and Ferrybridge C power stations to Edison Mission Energy, and entered into arrangements to supply coal to the stations for a four year period on terms consistent with Powergen's overall coal commitments.

Powergen also agreed to provide services associated with a major parts warranty in respect of the future operations, capability and availability of each station. Under the terms of the warranty, Powergen will have to repay up to £100 million per annum (£50 million per station) during each of the five years following the disposal should the plant be unavailable during the specified periods. The total consideration received from Edison Mission amounted to £1,296 million. £500 million of this amount was received in advance in respect of the provision of services under warranty arrangements and taken to deferred income. During 2000, £99 million of deferred income has been recognised within 'Other operating income' under these warranty arrangements.

Net assets disposed of, together with disposal costs, totalled £253 million, giving rise to an exceptional profit on disposal of £543 million, net of deferred income in respect of services under the warranty arrangements. A tax charge of £40 million arose on this disposal.

On 26 November 1998, Powergen North Sea Limited (PGNS) was sold to Centrica plc for consideration of £248 million in cash on a debt-free basis. Excluding inter-company debt, the net assets of PGNS on disposal were £252 million. On 31 December 1998, the Group sold a fifty per cent share in Powergen Renewables Limited (PGR) to Abbott plc for consideration of £5 million. The net assets of PGR disposed of totalled £3 million. The disposal of these two investments gave rise to a net £2 million loss.

Provision for loss on sale – International Operations

Following the decision to sell selected overseas assets, the carrying value of the Group's international asset portfolio has been reviewed. The value of its Indian and Australian assets has been reduced by £107 million, including goodwill written off of £48 million, to reflect the value implicit in the sale of these assets to companies which will be 80 per cent owned and managed by CLP Power International, a subsidiary of CLP Holdings Limited, and in which Powergen will retain a 20 per cent equity holding. This sale is expected to complete during 2001.

As part of the Group's strategy to refocus the business on the UK and US markets, its International Operations have been rationalised, and overseas offices closed. The amount of £26 million charged in these accounts principally comprises employee severance costs. £4 million of tax credits arise on this item.

4 Employee information

The average number of persons employed by the Group, including directors, analysed by activity was:

	Year ended 31 December 2000	Year ended 2 January 2000	Nine months ended 3 January 1999
UK Operations	**5,903**	7,130	5,560
US Operations*	**301**	–	–
International Operations	**830**	746	656
	7,034	7,876	6,216

* from 11 December 2000

At 31 December 2000, USOperations had 5,343 employees.

The salaries and related costs of employees, including directors, were:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Wages and salaries	**197**	224	131
Social security costs	**17**	19	10
Other pension costs (note 22)	**15**	16	11
	229	259	152
Capitalised in fixed assets	**(16)**	(24)	(13)
Charged in profit and loss account	**213**	235	139

Full details of the remuneration, pension arrangements and share options of the directors are set out in the Report on Directors' Remuneration and Related Matters on pages 19 to 23.

5 Net interest payable – Group

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Investment income	**1**	7	8
Interest receivable from associates and joint ventures	**7**	9	6
Interest receivable and similar income	**35**	40	9
	43	56	23
Interest payable:			
Bank loans and overdrafts	**(44)**	(55)	(48)
Other loans	**(146)**	(153)	(75)
	(190)	(208)	(123)
Net interest payable before unwinding of discount	**(147)**	(152)	(100)
Unwinding of discount in provisions	**(4)**	(4)	(4)
	(151)	(156)	(104)
Exceptional interest costs (note 3)	**(81)**	–	–
	(232)	(156)	(104)

6 Profit/(Loss) on ordinary activities before taxation

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
UK Operations			
Electricity and gas – wholesale and trading	**288**	448	264
Electricity – distribution	**116**	154	70
Electricity and gas – retail	**42**	3	17
Cogeneration and renewables	**18**	14	6
Other energy and hydrocarbon sales	–	–	9
Lease and other income	**182**	146	100
	646	765	466
US Operations*	**8**	–	–
International Operations	**121**	79	27
Corporate costs	**(47)**	(53)	(39)
Net interest payable:			
Group	**(151)**	(156)	(104)
Associates and joint ventures	**(60)**	(55)	(30)
Profit before goodwill amortisation and exceptional items	**517**	580	320
Goodwill amortisation	**(75)**	(68)	(28)
Exceptional items (note 3)	**26**	250	(537)
	468	762	(245)

* from 11 December 2000

Other energy and hydrocarbon sales represent the results of PGNS, a subsidiary company which was disposed of in November 1998.

The net assets of the Group are analysed as follows:

	The Group	
	At 31December 2000 £m	At 2 January 2000 £m
UK Operations	**3,007**	3,258
US Operations	**2,799**	–
International Operations	**571**	631
Unallocated net liabilities	**(4,091)**	(1,905)
	2,286	1,984

During the year, Powergen announced a number of asset disposals which had not completed by 31 December 2000 and are therefore not included in these accounts. These disposals include net assets for UK Operations of £186 million and for International Operations of £278 million.

7 Tax on profit on ordinary activities

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
United Kingdom corporation tax at 30% (year ended 2 January 2000 30.25% and nine months ended 3 January 1999 31%)			
Current	**5**	113	(97)
Prior year	**9**	(52)	(12)
	14	61	(109)
Overseas taxation	**(5)**	–	–
Deferred (note 24)			
Accelerated capital allowances	**72**	19	–
Other timing differences	**(61)**	(17)	14
	20	63	(95)
Associates and joint ventures	**7**	(13)	6
	27	50	(89)

The actual rate of tax reconciles with the applicable United Kingdom corporation tax rate as follows:

	Year ended 31 December 2000 %	Year ended 2 January 2000 %	Nine months ended 3 January 1999 %
United Kingdom corporation tax rate	**30**	30	31
Accelerated capital allowances	**14**	11	(1)
Other timing differences	**(15)**	(6)	2
Plant divestment	**(9)**	(6)	(6)
Prior year items	**2**	(9)	(4)
Net effect of different rates of tax in overseas businesses	**(4)**	–	–
Other	**(4)**	(3)	–
Effective tax rate on profit before exceptional items and goodwill amortisation	**14**	17	22
Exceptional items	**(8)**	(10)	14
Effective tax rate	**6**	7	36

The tax impact of exceptional items is given in note 3.

8 Dividends

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Net dividend per ordinary share:			
Interim paid			
10.8p (year ended 2 January 2000 10.8p, period ended 3 January 1999 10.0p)	**70**	70	65
Second interim proposed			
25.4p (year ended 2 January 2000 24.0p, period ended 3 January 1999 nil)	**166**	156	–
Final proposed			
£nil (year ended 2 January 2000 £nil, period ended 3 January 1999 14.1p)	–	–	92
	236	226	157

9 Profit of the Company

The profit for the financial year of the Company is £3,015 million (year ended 2 January 2000 £224 million, nine months ended 3 January 1999 £95 million). On 20 September 2000, the Company disposed of its non-voting 'B' ordinary shares in Powergen UK plc to Powergen Group Holdings, a fellow group undertaking. It retained £500 of voting 'A' ordinary shares. The consideration for the sale was £3,100 million in the form of ordinary and preference share capital issued at par by Powergen Group Holdings. A profit of £2,775 million arose as a result of this transaction, which is not distributable. The Company is not publishing a separate profit and loss account, as permitted by Section 230 of the Companies Act 1985.

10 Earnings per ordinary share

Earnings per ordinary share has been calculated by dividing the profit attributable to shareholders for the financial year of £429 million (year ended 2 January 2000 £708 million profit, nine months ended 3 January 1999 £156 million loss) by 650,976,860 ordinary shares (year ended 2 January 2000 649,552,248 ordinary shares, nine months ended 3 January 1999 646,681,662 ordinary shares), being the weighted average number of ordinary shares in issue during the year.

Earnings per ordinary share before goodwill amortisation and exceptional items based on the same numbers of weighted average ordinary shares is calculated as follows:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Profit/(Loss) attributable to shareholders	**429**	708	(156)
Goodwill amortisation	**75**	68	28
Exceptional items (net of tax)	**(70)**	(299)	379
Adjusted earnings	**434**	477	251
Earnings per share (before goodwill amortisation and exceptional items)	**66.7p**	73.4p	38.8p

Adjusted earnings per share has been presented in addition to earnings per share calculated in accordance with Financial Reporting Standard 14 'Earnings per Share' in order that more meaningful comparisons of financial performance can be made.

Diluted earnings per share is calculated as follows. The proceeds of the assumed exercise of dilutive Executive and ShareSave options is calculated as if the shares had been issued at fair value. The difference between the number of shares issued and the number of shares that would have been issued at fair value is treated as an issue of ordinary shares for no consideration. The number of shares used in the calculation of diluted earnings per share is shown on page 48.

11 Acquisitions

On 11 December 2000, the Group acquired the whole of the issued share capital of LG&E Energy Corp. (LG&E), a vertically integrated electricity and gas utility based in Louisville, Kentucky in the United States. The consideration payable totalled £2,258 million comprising £2,229 million in cash for shares together with capitalised acquisition costs totalling £29 million. The fair value of assets acquired was £760 million, leading to goodwill arising of £1,498 million. The transaction has been acquisition accounted.

On 10 October 2000, the Group acquired an additional 13.89 per cent stake in Gujarat Powergen Energy Corporation (GPEC) from Siemens Project Ventures GmbH for consideration of £34 million. The fair value of assets acquired was £40 million, leading to negative goodwill arising of £6 million. GPEC owns a 655MW dual-fired power station in Gujarat, North India. This purchase brought the Group's total stake in GPEC to 88 per cent. GPEC continues to be accounted for as a subsidiary undertaking.

On 29 September 2000, Powergen completed the purchase and sale of shares and related assets in Corby Power Limited (CPL) from Dominion Resources Inc. and ESBI Engineering (UK) Limited (ESBI). As a result of this transaction, CPL is now 50 per cent owned by Powergen and 50 per cent owned by ESBI. Following the acquisition, CPL has been treated as a joint venture by the Group. The consideration paid for this 50 per cent stake was £34 million and the fair value of net assets acquired was £50 million leading to negative goodwill arising of £16 million. CPL owns a 350MW gas-fired power station in the United Kingdom.

On 18 February 2000, Powergen acquired a 50 per cent stake in TeleCentric Solutions Limited (TCS), a joint venture with Affinity Internet Holdings plc, for consideration of £10 million. £5 million of the consideration was paid during 2000. The fair value of assets acquired was £1 million, leading to goodwill arising of £9 million.

The provisional calculation of goodwill arising on these acquisitions is shown on the next page. In view of the proximity of the acquisition of LG&E to the year end, further adjustments may arise.

	Book value £m	Accounting policy adjustments[(1)] £m	Revaluation[(2)] £m	Other fair value adjustments £m	Fair value to the Powergen Group £m
Net assets acquired:					
LG&E Energy Corp.					
Tangible fixed assets	2,724	193	(5)	–	2,912
Investments	222	(15)	(27)	–	180
Stocks	145	9	–	–	154
Taxation payable and deferred taxation	(406)	318	10	(5)	(83)
Other working capital	(408)	305	20	(2)	(85)
Net short-term borrowings	(851)	–	–	–	(851)
Long-term borrowings	(754)	(74)	14	–	(814)
Provisions	–	(484)	–	–	(484)
Minority interest	(169)	–	–	–	(169)
	503	252	12	(7)	760
Net assets acquired:					
GPEC					40
CPL					50
TCS					1
Goodwill					1,485
Consideration, including costs of acquisition					2,336

(1) The accounting policy adjustments made resulted from differences between Powergen's accounting policies under UK GAAP and US GAAP as followed by LG&E, including re-classification adjustments. The principal adjustments are as follows:

- Deferred taxation, provided for on a full liability basis under US GAAP, has been restated at the amount expected to crystallise in the foreseeable future. An adjustment of £199 million has been made to reverse that part of LG&E's deferred tax provision which is not required under UK GAAP.
- Decommissioning costs, where for regulated industries under US GAAP tangible fixed assets are depreciated to a negative amount equal to anticipated decommissioning costs and under UK GAAP the present value of anticipated decommissioning costs is included in provisions, added to tangible fixed assets and depreciated on a straight-line basis. Tangible fixed assets and provisions have been increased by £110 million and £75 million respectively.
- Regulatory assets and liabilities where, as explained in the principal accounting policies on page 30, there are specific rules in the US for accounting by utilities subject to rate regulation. There are no similar rules under UK GAAP and the criteria for recognition of assets and liabilities are different. Accordingly an adjustment has been made to reverse £28 million and £48 million of regulatory assets and liabilities respectively.
- Re-classification of assets and liabilities associated with US GAAP discontinued energy trading operations, presented in a single caption in the US GAAP balance sheet as a £301 million liability, to present each item under the relevant heading.

Other adjustments have been made to conform accounting policies on overhauls and software costs.

(2) Valuation adjustments have been made to the assets and liabilities of LG&E, principally to: write down the value of non-utility tangible fixed assets and investments to their recoverable amount (£27 million); reflect the fair values of the LG&E pension arrangements (£26 million liability); and, mark to market long-term debt based on interest rates at the date of acquisition (£14 million asset).

Pre-acquisition results – LG&E Energy Corp.

The unaudited results of LG&E and its subsidiaries prior to acquisition, prepared on the basis of its pre-acquisition accounting policies under US GAAP and excluding fair value adjustments are summarised below:

	Period to 10 December 2000 \$m	Year to 31 December 1999 \$m
Turnover	2,418	2,707
Operating profit	367	514
Net interest payable	(132)	(125)
Profit on ordinary activities before taxation	235	389
Tax on profit on ordinary activities	(81)	(134)
Profit on ordinary activities after taxation	154	255
Loss on disposal of discontinued operations net of tax benefit	(364)	(174)
Minority interest	(13)	(12)
(Loss)/Profit for the financial period	(223)	69
Preference dividends	(7)	(7)
(Loss)/Profit attributable to shareholders	(230)	62

There were no recognised gains and losses other than the (loss)/profit attributable to shareholders.

Post-acquisition results – LG&E Energy Corp.

The turnover and operating profit relating to LG&E and its subsidiaries (after goodwill amortisation) for the 21 days to 31 December 2000 under UKGAAP amounted to £116 million and £4 million (including £3 million of associates' and joint ventures' operating profit) respectively. The impact on Group cash flow for the same period was a £41 million contribution to net cash inflow from operating activities, interest payments of £6 million, taxation payments of £1 million, dividend payments of £22 million and payments of £27 million in respect of capital expenditure and financial investment.

12 Goodwill

The Group	£m
Cost	
At 2 January 2000	1,405
Acquisitions (note 11)	1,492
Disposals	(3)
Foreign exchange movements	(48)
At 31 December 2000	**2,846**
Amortisation	
At 2 January 2000	96
Charge for the year	75
Amounts written off	48
At 31 December 2000	**219**
Net book value at 31 December 2000	**2,627**
Net book value at 2 January 2000	1,309

Amortisation of goodwill for the 21 days to 31 December 2000 in respect of LG&E totalled £4 million, and is being amortised over its estimated useful economic life of 20 years.

Amounts written off goodwill relate to the sale of GPEC (see note 3).

13 Tangible fixed assets

The Group	Generating assets £m	Distribution and transmission networks £m	Other operating and short-term assets £m	Total £m
Cost				
At 2 January 2000	3,816	1,499	619	5,934
Foreign exchange movements	(55)	(58)	(18)	(131)
Acquired during the year	2,483	1,797	441	4,721
Additions	71	106	100	277
Transfers	40	(15)	(25)	–
Disposals	(271)	(2)	(45)	(318)
At 31 December 2000	**6,084**	**3,327**	**1,072**	**10,483**
Depreciation				
At 2 January 2000	1,985	524	193	2,702
Foreign exchange movements	(8)	(23)	(2)	(33)
Acquired during the year	976	727	106	1,809
Charge for the year	131	39	43	213
Transfers	4	(15)	11	–
Disposals	(221)	(2)	(39)	(262)
Exceptional write downs	11	–	79	90
At 31 December 2000	**2,878**	**1,250**	**391**	**4,519**
Net book value at 31 December 2000	**3,206**	**2,077**	**681**	**5,964**
Net book value at 2 January 2000	1,831	975	426	3,232

Group assets include freehold land and buildings with a net book value of £402 million (2 January 2000 £203 million) and assets in the course of construction at a cost of £539 million (2 January 2000 £291 million). Group assets also include assets held for use under operating leases with a cost of £132 million and accumulated depreciation of £132 million at both 31 December 2000 and 2 January 2000.

£7 million of interest was capitalised during the year (year ended 2 January 2000 £4 million and nine months ended 3 January 1999 £nil). Accumulated interest capitalised, gross of tax relief, included in the total cost for the Group amounts to £72 million (2 January 2000 £65 million, 3 January 1999 £61 million).

Assets held under finance leases are included in assets in the course of construction at a cost of £80 million.

14 Fixed asset investments

The Group	Net assets and goodwill: Joint ventures £m	Net assets and goodwill: Associates £m	Loans: Joint ventures £m	Loans: Associates £m	Other investments £m	Total £m
At 2 January 2000						
– net assets	7	329	38	26	70	470
– goodwill	–	–				–
Acquisition						
– net assets	102	120	–	–	9	231
– goodwill	(7)	–				(7)
Additions	–	13	1	23	19	56
Disposals	(2)	(37)	(7)	(29)	(18)	(93)
Exceptional write down	–	(48)	–	–	–	(48)
Retained profits	4	–	–	–	–	4
Currency translation differences	(2)	(11)	–	–	–	(13)
At 31 December 2000						
– net assets	**109**	**366**	**32**	**20**	**80**	**607**
– goodwill	**(7)**	–				**(7)**
	102	**366**	**32**	**20**	**80**	**600**

Additions to associated undertakings and joint ventures represent equity investments in, and loans to, associates and joint ventures respectively.

Goodwill arising on the acquisition of joint ventures includes £9 million of positive goodwill in respect of TCS, which is being amortised over ten years, and £16 million of negative goodwill in respect of CPL which is being amortised over 17 years. Aggregate amortisation of goodwill of associates and joint ventures as at 31 December 2000 was £nil, therefore the net book value of that goodwill at both 2 January 2000 and 31 December 2000 was equal to its cost.

Other investments include investments listed on a recognised stock exchange of £69 million (year ended 2 January 2000 £70 million) set aside by subsidiary companies for certain medium and long-term insurance liabilities. At 31 December 2000, the market value of these investments was £3 million in excess of cost (2 January 2000 £1 million). These Sterling investments can be analysed under US GAAP as follows:

	At 31 December 2000 Carrying value £m	At 31 December 2000 Fair value £m
Equity investments	26	26
Debt investments	43	46
Total	69	72

Proceeds from the sale of investments classified as 'available for sale' under US GAAP amounted to £112 million for the year ended 31 December 2000. On these sales gross realised profits and losses amounted to £2 million and £2 million respectively. These gains and losses were computed by reference to the actual cost of the specific securities being sold.

The contracted maturity of the Group's debt investments at 31 December 2000 was as follows:

	£m
Within one year	12
1–5 years	10
5–10 years	15
After 10 years	6
Total	43

The Company

On 20 September 2000, Powergen plc set up a new wholly owned subsidiary, Powergen Group Holdings, an unlimited liability company. On the same date, the Company disposed of its non-voting 'B' ordinary shares to Powergen Group Holdings (see note 9). The cost of investment in the Company balance sheet at 31 December 2000 of £3,100 million represents the 100 per cent ownership of this subsidiary undertaking, together with a £500 investment in Powergen UK plc. The cost of investment of £325 million in the Company balance sheet at 2 January 2000 represented a 100 per cent interest in Powergen UK plc.

Interests in Group subsidiary undertakings

Details of the Group's principal investments in subsidiary undertakings are set out below. Principal subsidiaries are those which in the opinion of the directors significantly affect the amount of profit and assets and liabilities shown in the Group accounts. The directors consider that those companies not listed are not significant in relation to Powergen as a whole.

	Proportion of nominal value of issued equity shares held by the Group or the Company %	Country of incorporation or registration	Principal business activities
Powergen Group Holdings*	100	England & Wales	Holding company for UK based activities
Powergen US Holdings Limited*	100	England & Wales	Holding and financing company for US based activities
Powergen UK plc†	100	England & Wales	Generation and sale of electricity
LG&E Energy Corp. (LG&E)†	100	United States	Holding company for US based activities
Louisville Gas and Electric Company (LGEC)†	100	United States	Generation and distribution of electricity and supply of electricity and gas
Kentucky Utilities Company (KU)†	100	United States	Generation, distribution and supply of electricity
LG&E Capital Corp.†	100	United States	Holding company for US based non-utility activities
Powergen Energy plc†	100	England & Wales	Distribution and supply of electricity
Powergen International Limited†	100	England & Wales	Holding company for international activities

	Proportion of nominal value of issued equity shares held by the Group or the Company %	Country of incorporation or registration	Principal business activities
Ergon Insurance Limited†	100	Isle of Man	Captive insurance company
Powergen CHP Limited†	100	England & Wales	Sale of energy services involving the construction of combined heat and power (CHP) plant
Powergen Cogeneration Limited†	100	England & Wales	Sale of energy services involving the construction of combined heat and power (CHP) plant
Powergen Gas Limited†	100	England & Wales	Transportation and marketing of gas in the UK
Powergen Retail Gas Limited†	100	England & Wales	Supply, trading and shipping of gas in the UK
Csepeli Aramtermelo Rt†	100	Hungary	Generation and sale of electricity
Csepel Power Company†	100	Hungary	Generation and sale of electricity
Gujarat Powergen Energy Corporation Limited (GPEC)†	88	India	Generation and sale of electricity

* direct interest † indirect interest

All the above subsidiaries have a December year end apart from GPEC, which, for commercial reasons, has an accounting reference date of 31 March.

Associated undertakings and joint ventures

Details of the Group's principal investments in associated undertakings and joint ventures are as follows:

	Accounting reference date	Country of incorporation or registration	Shares held	Percentage of capital held directly by the Group
Saale Energie GmbH	31 December	Germany	Deutschmark ordinary capital	50%
MIBRAG BV	31 December	Netherlands	Dutch guilders ordinary capital	33.33%
MIBRAG GmbH	31 December	Germany	Deutschmark ordinary capital	33.33%
Turbogas Produtora Energetica SA	31 December	Portugal	Escudos ordinary shares	49.99%
PT Jawa Power	31 December	Indonesia	Indonesian rupees ordinary shares	35%
Yallourn Energy Pty Limited	30 June	Australia	Australian dollar ordinary shares	49.95%
Distribuidora de Gas Cuyana	30 November	Argentina	Argentinian peso ordinary shares	14.4%
Gas Natural BAN SA	30 September	Argentina	Argentinian peso ordinary shares	19.5%
LG&E Power Gregory*	30 November	United States	Partner	50%
Corby Power Limited*	30 September	England & Wales	Ordinary shares	50%
Cottam Development Centre Limited*	31 December	England & Wales	Ordinary shares	50%
TeleCentric Solutions Limited*	31 December	England & Wales	Ordinary shares	50%

* treated as joint ventures in the Group's accounts

The principal activities of these associated undertakings and joint ventures are:

Saale Energie GmbH	–	Holding and management company for the Group's interest in Schkopau power station
MIBRAG BV	–	Holding company for the Group's interest in MIBRAG GmbH
MIBRAG GmbH	–	Mining, refinement and sale of brown coal and generation and sale of electricity
Turbogas Produtora Energetica SA	–	Generation and sale of electricity from gas-fired power station
PT Jawa Power	–	Generation and sale of electricity from coal-fired power station
Yallourn Energy Pty Limited	–	Mining of brown coal and production and sale of electricity from coal-fired power station
Distribuidora de Gas Cuyana	–	Sale and distribution of gas
Gas Natural BAN SA	–	Sale and distribution of gas
LG&E Power Gregory	–	Owns and operates gas-fired power station
Corby Power Limited	–	Generation and sale of electricity from gas-fired power station
Cottam Development Centre Limited	–	Construction and operation of gas-fired power station plant and operation of a generator turbine testing facility
TeleCentric Solutions Limited	–	Retail of telecommunications services and development of multi-utility billing system

Group share of aggregate associates' and joint ventures' balance sheets and results

	At 31 December 2000		At 2 January 2000	
	Joint ventures £m	**Associates £m**	Joint ventures £m	Associates £m
Share of assets:				
Share of fixed assets	**316**	**1,601**	46	1,533
Share of current assets	**127**	**176**	3	163
	443	**1,777**	49	1,696
Share of liabilities:				
Amounts falling due within one year	**(46)**	**(143)**	(1)	(133)
Amounts falling due after more than one year	**(295)**	**(1,268)**	(41)	(1,234)
	(341)	**(1,411)**	(42)	(1,367)
Share of net assets	**102**	**366**	7	329
Turnover	**49**	**245**	10	233
Operating profit	**10**	**63**	2	81

15 Stocks

	The Group	
	At31December 2000 £m	At 2 January 2000 £m
Fuel stocks	**129**	70
Stores	**129**	57
	258	127

16 Debtors: amounts falling due after more than one year

	The Group	
	At31December 2000 £m	At 2 January 2000 £m
Other debtors	**125**	11

Other debtors include £4 million in respect of pensions (2 January 2000 £5 million) and £51 million (2 January 2000 £nil) in respect of income under operating leases.

17 Debtors: amounts falling due within one year

	The Group	
	At 31 December 2000 £m	At 2 January 2000 £m
Trade debtors	**838**	484
Less: securitisation	**(152)**	–
Net trade debtors	**686**	484
Other debtors	**178**	204
Prepayments and accrued income	**45**	34
	909	722

Other debtors include £31 million (2 January 2000 £70 million) in respect of income under operating leases.

The Company has no debtors apart from £181 million (2 January 2000 £161 million) of inter-group balances due from subsidiaries. On 15 December 2000, Powergen launched a revolving-period £300 million securitisation programme to sell all of its right, title and interest in certain billed and unbilled trade debtors (for electricity and gas retail customers) to Kittyhawk Funding Corporation, a trust established for the purpose of purchasing these trade debtors from Powergen. The trust then sells the trade debtors to outside investors. Interest is charged on the amounts borrowed under the securitisation programme at a margin above LIBOR, and is payable monthly. Powergen is not obliged to support any loss suffered by the trust or the related investors as a result of the securitisation programme, and does not intend to do so. The trust has agreed not to seek recourse against any other assets, apart from the identified billed and unbilled trade debtors. Powergen has an option to repurchase defaulted debt from the trust for a nominal sum.

At 31 December 2000, amounts advanced by the trust to the Group totalled £300 million, of which £152 million was backed by billed and unbilled trade debtor balances. These trade debtors were accounted for as a sale under US GAAP Statement of Financial Accounting Standards 125 'Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities'. USGAAP would therefore present the trade debtors figures on a net basis. Powergen retains the responsibility for servicing these trade debtors. The remaining £148 million advanced by the trust is included in loans and overdrafts within creditors due within one year.

18 Loans and overdrafts

	Weighted average interest rate		The Group	
	Year ended 31 December 2000 %	Year ended 2 January 2000 %	At 31 December 2000 £m	At 2 January 2000 £m
UK:				
Bank overdrafts	–	–	**3**	37
Other short-term loans	**8.0**	7.3	**1,839**	61
Commercial paper	**6.6**	–	**33**	–
	8.0	7.3	**1,875**	98
US:				
Short-term loans	**7.1***	–	**428**	–
	7.9	**7.3**	**2,303**	98

* from 11 December 2000

UK short-term loans shown above include £1,131 million of debt relating to the acquisition of LG&E drawn down under a US $4,000 million facility (see note 20).

The Group has two commercial paper programmes, as follows:

	Euro programme	US Dollars programme
Maximum amount permitted	US $500 million	US $3,000 million
Repayment periods	7 – 364 days	1 – 270 days
Amount outstanding:		
31 December 2000	–	£33m
2 January 2000	–	N/A
Basis of interest rate	Currency of issue LIBOR	US LIBOR

The US $3,000 million programme was signed on 18 December 2000.

19 Trade and other creditors falling due within one year

	The Group	
	At 31 December 2000 £m	At 2 January 2000 £m
Trade creditors	**705**	393
Payments on account	–	11
Corporation tax	**144**	86
Other taxation and social security	**70**	9
Accruals and other creditors	**389**	351
Deferred income	**100**	100
Proposed dividend	**166**	156
	1,574	1,106

Accruals and other creditors include accruals for capital work performed but not yet paid for and rationalisation and restructuring costs of the Group. The Company has no trade and other creditors apart from the proposed dividend of £166 million (2 January 2000 £156 million).

20 Long-term loans

	The Group	
	At 31 December 2000 £m	At 2 January 2000 £m
UK:		
7.1% US Dollar Yankee Bond 2002	**252**	253
Sterling term facility expiring 2003	–	299
8.875% Sterling Bond 2003	**250**	250
US Dollar term facility expiring 2005	**1,004**	–
8.5% Sterling Bond 2006	**250**	250
8.375% Sterling Eurobond 2006	–	106
8.125% Sterling Eurobond 2007	–	105
7.45% US Dollar Yankee Bond 2007	**260**	262
Loan notes 2007	**4**	4
5% Euro Eurobond 2009	**326**	326
12% Sterling Eurobond 2016	–	224
6.25% Sterling Eurobond 2024	**244**	244
US:		
6.205% Medium term US Dollar notes 2004	**96**	–
6.46% Medium term US Dollar notes 2008	**91**	–
First mortgage bonds 2003 – 2027 (secured)	**184**	–
Pollution control bonds 2010 – 2027 (secured)	**340**	–
Finance lease obligations	**80**	–
Other:		
Bank loans in other overseas subsidiaries	**247**	249
	3,628	2,572

The Sterling term facility expiring in 2003 bears interest at variable rates, fixed in advance for periods up to six months, by reference to Sterling LIBOR. The US Dollar term facility was signed on 27 February 2000 and expires on 27 February 2005. It bears interest at variable rates fixed in advance for periods up to six months, by reference to US LIBOR.

All finance lease obligations fall due on 31 December 2004. The obligation of £80 million above includes £3 million of interest.

None of the bonds outstanding at 31 December 2000 has any financial covenants except for dividend restrictions on the first mortgage and pollution control bonds. Substantially all of LGEC's and KU's utility plants are pledged as security for its first mortgage bonds.

On 28 December 2000, Powergen redeemed the 8.375 per cent Sterling Eurobond 2006, the 12 per cent Sterling Eurobond 2016 and the 8.125 per cent Sterling Eurobond 2007 at a cost of £493 million funded from a combination of cash and existing bank facilities. These three Sterling Eurobonds were inherited with the acquisition of East Midlands Electricity plc in July 1998. The premium paid of £66 million has been treated as an exceptional cost in these accounts (see note 3).

The maturity profile of the Group's financial liabilities, including overdrafts and long-term loans, is as follows:

	At31December 2000 £m
In one year or less, or on demand	**2,303**
In more than one year but not more than two years	**277**
In more than two years but not more than five years	**1,573**
In more than five years	**1,778**
	5,931

The undrawn committed borrowing facilities available to the Group are as follows:

	At31December 2000 £m
Expiring in one year or less	**286**
Expiring in more than two years but not more than five years	**1,300**
	1,586

These facilities comprise:

Facility	Amount undrawn at 31 December 2000 £m	Expiry date	Fees	Covenants
US $4,000 million facility:				
– 364 day extendable loan	542	27 February 2005	20 bps	£7,250 million cap on total Group borrowings, maximum net debt to EBITDA ratio of 5.5 times, minimum EBITDA to interest ratio of 2.1 times
– 5 year revolving credit facility	–	27 February 2005	55 bps	
– 5 year term loan	–	27 February 2005	55 bps	
Syndicated Sterling loan facility:				
– 5 year revolving credit facility	465	26 June 2003	20 bps	UK plc consolidated sub-group £3,500 million cap on total borrowings, maximum net debt to EBITDA ratio of 4.25 times, minimum PBIT to interest ratio of 2.25 times
LG&E Capital Corp. lines of credit	121	August 2001	10 bps	Tangible net worth at least US $25m
LG&E Capital Corp. lines of credit	293	September 2002	7.5 bps	Adjusted capitalisation ratio not to exceed 70 per cent
Louisville Gas and Electric Company line of credit	134	November 2001	7.5 bps	–
UK committed bi-lateral facility	25	Expired 18 January 2001	–	–
Committed facilities in overseas subsidiaries	6	Expired 2 February 2001	–	–
	1,586			

21 Other creditors falling due after more than one year

	The Group	
	At31December 2000 £m	At 2 January 2000 £m
Accruals and other creditors	**237**	75
Deferred income	**240**	340
	477	415

Accruals and other creditors shown above include £106 million in respect of pensions (2 January 2000 £57 million).

22 Pension scheme arrangements and other post-retirement benefits

a) Pension scheme arrangements

At 31 December 2000, Powergen had both statutorily approved defined benefit pension schemes and several smaller statutorily approved defined contribution plans. Details of the LG&E arrangements are included following the acquisition of that company and its subsidiaries on 11 December 2000. The pension charge in respect of LG&E included in the Group's results is for the period 11 December 2000 to 31 December 2000 only.

UK GAAP

The Group participates in the industry-wide scheme, the Electricity Supply Pension Scheme (ESPS), for the majority of its UK based employees. This is a funded scheme of the defined benefit type, with assets invested in separate trustee administered funds. The Group has two separate funds with the ESPS, the Powergen UK fund and the East Midlands Electricity fund. An actuarial valuation of the ESPS is normally carried out every three years by the Scheme's independent, professionally qualified, actuary, who recommends the rates of contribution payable by each group participating in the scheme. In intervening years the actuary reviews the continuing appropriateness of the rates.

The latest published actuarial valuation of the ESPS was at 31 March 1998. The 1998 valuation revealed a surplus of £89 million in respect of the Powergen fund and £32 million in respect of the East Midlands Electricity fund.

	At 31 March 1998	
	Powergen UK fund	East Midlands Electricity fund
Market value of assets	£1,631m	£881m
Extent to which actuarial value covered benefits accruing to members	108%	105%
Rate of return on investments:		
– compared with annual increase in salaries	2.5% higher	2.5% higher
– compared with annual increase in pensions	4.0% higher	4.0% higher
Method of valuation used	Projected unit	Attained age

Following the acquisition of LG&E on 11 December 2000, the associated US pension arrangements are included in these accounts. LG&E sponsors a number of qualified and non-qualified pension plans, the majority of which are funded schemes of the defined benefit type. An actuarial valuation of the plans is carried out annually by an independent, professionally qualified, actuary. Current year values have been based on the valuation at 31 December 1999 and have been adjusted for any known movements during the year. There are no plan assets in the non-qualified plans.

	At 31 December 2000
	LG&E funds
Market value of assets	£395m
Extent to which actuarial value covered benefits accruing to members	101%
Rate of return on investments:	
– compared with annual increase in salaries	5.5% higher
– compared with annual increase in pensions	–
Method of valuation used	Projected unit

Pension costs for the Group

In the financial year ended 31 December 2000, the normal pension cost for the Group amounted to £20 million (year ended 2 January 2000 £21 million, nine months ended 3 January 1999 £13 million). A net credit of £5 million (year ended 2 January 2000 £5 million, nine months ended 3 January 1999 £2 million) is required to the pension charge in the accounts in respect of the experience surplus on the pension schemes, which is being recognised over 13 years, the average remaining service lives of members. The accounts include a prepayment of £23 million (2 January 2000 £18 million) representing the excess of the amounts funded over the pension cost for the year.

Amounts set aside in other creditors for the Group's rationalisation and restructuring programme in the UK include costs associated with the early retirement of employees. An element of these costs is likely to be payable to the ESPS to meet early retirement costs.

US GAAP

The effect of adopting US Statements of Financial Accounting Standards (SFAS 87 and SFAS 88) is shown on page 47.

The pension cost determined under SFAS 87 requirements for the three periods ended 31 December 2000 and the projected benefit obligation as at 31 December 2000 were calculated using the following assumptions:

	Projected benefit obligation		Pension cost			
	At 31 December 2000 Powergen Group excluding LG&E	**At 31 December 2000 LG&E**	**Year ended 31 December 2000**	Year ended 2 January 2000	Nine months ended 3 January 1999	Five months ended 3 January 1999
	%	**%**	**%**	%	%	%
Discount rate	**5.0**	**7.5**	**5.0**	4.5	6.75	6.0
Rate of future salary increases	**4.0**	**4.0**	**4.0**	4.0	5.5	5.0
Rate of expected return on plan assets	**6.5**	**9.5**	**6.5**	6.5	8.0	7.5

The figures for the five months ended 3 January 1999 were used to reflect the inclusion of Powergen Energy plc in the Group's pension disclosures from the date of acquisition.

The components of the schemes' pension cost under SFAS 87 are as follows:

Change in benefit obligations

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Benefit obligation at start of year	**2,162**	2,304	1,285
Powergen Energy on acquisition	**–**	–	781
LG&E on acquisition	**404**	–	–
Service cost	**17**	31	13
Interest cost	**136**	105	85
Plan participants' contributions	**9**	11	5
SFAS 88 events	**38**	9	10
Actuarial (gain)/loss	**–**	(179)	196
Benefits paid	**(129)**	(119)	(71)
Disposal of business	**(9)**	–	–
Foreign exchange	**(13)**	–	–
Benefit obligation at end of year	**2,615**	2,162	2,304

Change in plan assets

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Market value of plan assets at start of year	**2,876**	2,522	1,631
Powergen Energy on acquisition	**–**	–	843
LG&E on acquisition	**412**	–	–
Actual return on plan assets	**25**	455	93
Employer contributions	**36**	7	21
Plan participants' contributions	**9**	11	5
Total payments	**(129)**	(119)	(71)
Disposal of business	**(8)**	–	–
Foreign exchange	**(13)**	–	–
Market value of plan assets at end of year	**3,208**	2,876	2,522

Components of net periodic pension cost

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Cost of benefits earned during the year	**17**	31	13
Interest cost on projected benefit obligation	**111**	105	85
Expected return on assets	**(188)**	(165)	(124)
Net amortisation	**(21)**	2	(10)
Pension credit for the year under US GAAP	**(81)**	(27)	(36)

Additional pension costs in relation to severances under SFAS 88 are as follows:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Cost of termination benefits	**38**	9	10

The information required to be disclosed in accordance with SFAS 87 concerning the funded status of the Powergen UK and East Midlands Electricity funds of the ESPS, and the various LG&E funds, at 31 December 2000 and 2 January 2000 was as follows:

	At31December 2000 £m	At 2 January 2000 £m
Projected benefit obligations	**2,615**	2,162
Plan assets at market value	**3,208**	2,876
Projected benefit obligation less plan assets	**(593)**	(714)
Reconciliation of plans' status:		
Unrecognised net obligation at date of initial application of SFAS 87*	**–**	(2)
Unrecognised net gain	**402**	583
Unrecognised prior service cost	**(23)**	–
Net accrued pension credit under US GAAP	**(214)**	(133)

* the unrecognised net obligation at the date of initial application is being amortised over 15 years

The schemes' assets are invested in UK and overseas equities, index-linked bonds and property.

b) Other post-retirement benefits

LG&E provides healthcare and other benefits through various plans for eligible retirees on a basis substantially similar to those who are active employees. The cost of post-retirement benefits is accrued over the active service lives of employees.

In the financial year ended 31 December 2000, the cost in respect of post-retirement healthcare amounted to £1 million. This amount was only in respect of the LG&Egroup for the 21 days ended 31 December 2000. There was a creditor of £41 million in respect of post-retirement healthcare arrangements.

The net periodic post-retirement benefit cost and significant assumptions in respect of the period from the date of acquisition, 11 December 2000, to 31 December 2000 are summarised as follows:

	Period ended 31 December 2000 %
Discount rate	**8.0**
Initial healthcare cost trend rate – under 65	**8.0**
Initial healthcare cost trend rate – over 65	**8.0**
Ultimate healthcare cost trend rate	**5.0**

The majority of the plans are funded schemes of the defined benefit type. An actuarial valuation of the plans is carried out annually by an independent, professionally qualified, actuary, on a projected unit basis. Current year values have been based on the valuation at 31 December 1999 and have been adjusted for any known movements during the year.

The change in the accumulated post-retirement benefit obligation, change in plan assets and funded status are as follows:

Change in accumulated post-retirement benefit obligation

	Period ended 31 December 2000 £m
Accumulated post-retirement benefit obligation on acquisition	**85**
Foreign exchange	**(2)**
Accumulated post-retirement benefit obligation at end of year	**83**

The plan assets were valued at £21 million at both 11 December 2000 and 31 December 2000, giving a funding level of 25 per cent.

Post-retirement benefit plans in the US are not usually funded. In US regulated industries such as LG&E's however, this funding level of 25 per cent is typical.

Reconciliation of accrued post-retirement benefit cost and total amount recognised

	Period ended 31 December 2000 £m
Funded status of plan	**(62)**
LG&E unrecognised net gain	**21**
Accrued post-retirement benefit cost	**(41)**

The assumed healthcare cost trend rate gradually decreases over five years and remains level thereafter. The healthcare cost trend rate assumption has a significant effect on the amounts reported. Increasing the assumed healthcare cost trend rate by one percentage point would have increased the accumulated post-retirement benefit obligation (APBO) as at 31 December 2000 by £7 million, and the net periodic post-retirement benefit costs by £1 million. Decreasing the assumed healthcare cost trend rate by one percentage point would have reduced the APBO as at 31 December 2000 by £6 million, and the net periodic post-retirement benefit costs by £1 million.

23 Provisions for liabilities and charges

Movements on provisions comprise:

	2 January 2000 £m	Acquired during the year £m	Charged to profit and loss account £m	Amortisation of discount £m	Provisions utilised £m	Provisions released or disposed £m	Exchange movements £m	**31 December 2000 £m**
US contract provisions	–	409	–	–	(8)	–	(13)	**388**
UK contract provisions	150	–	–	–	(13)	–	–	**137**
Liability and damage claims	71	–	8	–	(12)	(7)	–	**60**
Decommissioning	74	75	2	4	(1)	(5)	(3)	**146**
	295	484	10	4	(34)	(12)	(16)	**731**

US contract provisions relate to out of money fixed price energy marketing contracts entered into in 1996 and 1997 by LG&E. These contracts were acquired by Powergen on the purchase of LG&E on 11 December 2000. The provisions will be utilised over the period to 2008. UK contract provisions, which relate to out of money electricity purchase contracts, were acquired on the purchase of Powergen Energy plc and will be utilised over the period to 2008, when the contract terminates. The liability and damage claims provision includes reserves in respect of future claims for industrial related diseases and gradual pollution. Given the inherent uncertainty surrounding the timing of any potential claims, it is not possible to estimate when these amounts will crystallise. Decommissioning provisions comprise amounts set aside for the estimated costs of terminating power station grid connections, decommissioning power stations and subsequent site restoration costs at UK and US power stations which will be utilised as each power station closes.

24 Deferred tax

An analysis of the full potential liability and the net deferred tax liability recognised at 31 December 2000 under UK GAAP is as follows:

	31 December 2000			2 January 2000		
	Full potential liability £m	**Amounts unprovided £m**	**Liability/ (Asset) recognised £m**	Full potential liability £m	Amounts unprovided £m	Liability/ (Asset) recognised £m
Accelerated capital allowances	**933**	**(801)**	**132**	525	(476)	49
Other timing differences	**(266)**	**227**	**(39)**	(134)	132	(2)
	667	**(574)**	**93**	391	(344)	47

Where there is an intention that profits retained by overseas subsidiaries will be remitted, provision is made for any taxation liability that would arise on the distribution. No provision is made where there is no intention that such profits will be remitted in the foreseeable future. Assets and liabilities have been recognised for those timing differences that are expected to crystallise in the foreseeable future. The liability in respect of accelerated capital allowances and other timing differences is calculated at 30 per cent in both periods.

25 Share capital

The share capital of the Company comprises:

Authorised	31 December 2000 £m	2 January 2000 £m
1,050,000,000 ordinary shares of 50p each	**525**	525
49,998 redeemable preference shares of £1	–	–
Special rights redeemable preference share of £1	–	–
	525	525
Allotted, called-up and fully paid		
651,494,671 (2 January 2000 649,726,502) ordinary shares of 50p each	**326**	325
49,998 redeemable preference shares of £1	–	–
Special rights redeemable preference share of £1	–	–
	326	325

During the year 478,582 ordinary shares of 50p each were issued under the Powergen ShareSave Scheme realising £1,878,120. An amount of £1,638,829 has been credited to share premium account. A further 9,256 shares held by a Qualifying Employee Share Trust (Quest) were also exercised during the year. The number of shares held by the Quest at 31 December 2000 was 258, on which dividends had been waived (2 January 2000 9,514 shares on which dividends had not been waived).

During the year 212,250 ordinary shares of 50p each were issued under the Powergen Executive Share Option Scheme realising £980,382. An amount of £874,257 has been credited to share premium account.

During the year 1,077,337 ordinary shares of 50p each were issued under the Powergen Profit Sharing Share Scheme realising £3,856,866. An amount of £3,318,198 has been credited to share premium account.

The special rights redeemable preference share held by the Secretary of State or another person acting on behalf of HM Government since privatisation, was redeemed for consideration of £1 on 22 December 2000.

The redeemable preference shares are held by Powergen UK plc and are redeemable at par at the option of Powergen plc. The holders of the limited-voting redeemable preference shares are not entitled to receive or participate in any of the profits of the Company available for distribution by way of dividend or otherwise.

Share option schemes

The Company has two share option schemes under which options to acquire shares have been granted to employees; the Powergen ShareSave Scheme, which is available to all eligible Group employees, and the Powergen Executive Share Option Scheme, which is available to executive directors and other senior executives and managers selected by the Remuneration Committee.

The Powergen ShareSave Scheme is savings related and the share options are normally exercisable on completion of a three or five year Save-As-You-Earn (SAYE) contract. The exercise price of options granted may be at a discount of no more than 20 per cent of the market price at the date of the grant.

Under the Powergen Executive Share Option Scheme, which the Company regards as an important incentive in attracting and retaining key employees, the share options are generally exercisable between the third and tenth anniversaries of the date of grant. Options are granted at the market price of the Company's shares at the time of the grant or higher where options have previously been exercised at a higher rate. Options granted after 1994 are subject to specific performance criteria having been met at the time of exercise, as established by the Remuneration Committee. For this purpose the performance of the Company is assessed in terms of Total Shareholder Return as compared against other companies which constitute the FTSE 100 at the date of each grant.

The number of ordinary shares issued or issuable pursuant to options granted under the ShareSave Scheme and the Executive Share Option Scheme shall not exceed 117,188,722 (representing 15 per cent of the issued ordinary share capital of the Company immediately following the date on which the Company's shares were first admitted to the Official List of The Stock Exchange) for either scheme.

Options granted, exercised and lapsed under these share option schemes during the three financial periods ended 31 December 2000 were as follows:

	Powergen ShareSave Scheme		Powergen Executive Share Option Scheme	
	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise price
Outstanding at 29 March 1998	6,672,149	£4.14	2,201,000	£5.46
Granted	–	–	403,000	£8.88
Exercised	(1,291,323)	£3.11	(343,500)	£4.93
Lapsed	(157,573)	£4.66	–	–
Outstanding at 3 January 1999	5,223,253	£4.38	2,260,500	£6.15
Granted	3,162,793	£6.02	471,500	£7.10
Exercised	(778,072)	£3.84	(52,600)	£4.69
Lapsed	(470,937)	£5.25	(16,500)	£7.35
Outstanding at 2 January 2000	7,137,037	£5.11	2,662,900	£6.34
Acquisition	–	–	4,915,060	£5.67
Granted	7,007,440	£2.95	2,901,000	£4.00
Exercised	(487,838)	£3.92	(212,250)	£4.62
Lapsed	(5,007,230)	£5.37	(500)	£3.87
Outstanding at 31 December 2000	**8,649,409**	**£3.28**	**10,266,210**	**£5.39**

Options outstanding at 31 December 2000, together with their exercise prices and dates of exercise, are as follows:

			Number of ordinary shares	
Date of grant	Price per share £	Normal dates of exercise	31 December 2000	2 January 2000
Powergen ShareSave Scheme:				
24 July 1996	3.77	1999 & 2001	**1,556,907**	2,758,796
25 July 1997	5.81	2000 & 2002	**165,979**	1,433,554
1 June 1999	6.02	2002	**345,772**	2,944,687
1 June 2000	2.95	2003	**6,580,751**	–
Powergen Executive Share Option Scheme:				
6 December 1991	2.21	1994–2001	**16,500**	40,000
1 December 1992	2.78	1995–2002	**92,000**	107,000
1 July 1993	3.87	1996–2003	**59,500**	82,000
22 November 1994	5.57	1997–2004	**223,450**	261,500
5 July 1995	4.86	1998–2005	**23,800**	28,000
5 July and 29 November 1995	5.32	1998–2005	**244,600**	292,500
29 November 1995	5.59	1998–2005	**15,500**	15,500
26 June 1996	4.705	1999–2006	**90,300**	111,900
26 June 1996	5.32	1999–2006	**246,500**	286,500
26 June 1996	5.34	1999–2006	**11,000**	11,000
26 June 1996	5.59	1999–2006	**16,500**	16,500
11 December 1996	5.72	2001–2006	**78,500**	78,500
2 July 1997	7.35	2000–2007	**457,500**	457,500
25 September 1998	8.88	2001–2008	**403,000**	403,000
12 March 1999	7.10	2002–2009	**471,500**	471,500
10 April 2000	3.995	2003–2010	**2,901,000**	–
11 December 2000	5.672	2000–2010	**4,915,060**	–

The Company had options exercisable totalling 1,101,478, 1,261,656 and 872,930 and shares available for the grant of options totalling 215,461,825, 224,577,507 and 226,893,591 at 31 December 2000, 2 January 2000, and 3 January 1999 respectively. No options expired during the three financial periods ended 31 December 2000.

US GAAP – Fair value of options

The weighted average fair value of options granted at a discount during the year to 31 December 2000 was £1.02 (year to 2 January 2000 £1.45). The weighted average fair value of options granted at a premium during the year to 31 December 2000 was £0.82 (year to 2 January 2000 £0.85). The weighted average fair value of options granted at market price during the year to 31 December 2000 was £0.99 (year to 2 January 2000 £nil). The weighted average remaining contractual life of options outstanding at 31 December 2000 was 2.4 years. The fair value of options granted under each scheme is estimated using the Black Scholes options pricing model with the following weighted average assumptions for grants in the year to 31 December 2000: expected volatility – 37 per cent; interest rates – 5.5 per cent (based upon UK Gilts on the date of grant with a maturity equal to the expected term); expected dividend yield – 6.5 per cent and expected term – 3 years for the ShareSave Scheme and 4 years for the Executive Share Option Scheme.

The Company has adopted the disclosure only option under SFAS 123, 'Accounting for Stock Based Compensation'. If the accounting provisions of that standard had been adopted, Powergen's net income and earnings per share under US GAAP would be as the pro-forma amounts indicated below:

	31 December 2000	2 January 2000
Net income – as reported	**£430m**	£1,125m
– pro-forma	**£426m**	£1,122m
Earnings per share – as reported	**66.1p**	173.2p
– pro-forma	**65.4p**	172.7p

The determination of stock option compensation under USGAAP is measured in accordance with Accounting Principles Board (APB) Opinion 25 'Accounting for Stock Issued to Employees'.

26 Reserves

The Group	Share premium account £m	Other reserves £m	Revaluation reserve £m	Profit and loss account £m
At 2 January 2000	4	656	25	909
Premium on shares issued	5	–	–	–
Currency translation differences on foreign currency net investments	–	–	–	(32)
Transfers	–	–	(2)	2
Retained profit for the year	–	–	–	193
At 31 December 2000	**9**	**656**	**23**	**1,072**

The element of 'other reserves' relating to the previous capital reserve of £474 million, is not available for distribution as long as any liabilities of Powergen as at 9 December 1998 remain undischarged, unless the persons to whom such liabilities are owed shall otherwise agree, or an appropriate bank guarantee of such liabilities is put in place.

On 27 July 1999, the Group acquired an additional 46.3 per cent stake in GPEC, formerly an associated undertaking. In accordance with Financial Reporting Standard 2 'Accounting for Subsidiary Undertakings', and in order to give a true and fair view, purchased goodwill was calculated as the sum of the goodwill arising on each separate purchase of shares in GPEC. The increase, from the value of the associate stake in GPEC to the fair value of that stake on 27 July 1999, gave rise to the £25 million revaluation reserve shown above.

Aggregate goodwill written off directly to the Group profit and loss reserve totals £16 million (2 January 2000 £16 million).

The Company	Profit and loss account £m
At 2 January 2000	1
Profit attributable to shareholders	3,015
Dividends	(236)
At 31 December 2000	**2,780**

Of the £2,780 million profit and loss reserve at 31 December 2000, £2,775 million is not distributable (see note 9).

27 Minority interests

	31 December 2000			2 January 2000		
	Equity £m	Non-equity £m	Total £m	Equity £m	Non-equity £m	Total £m
Opening minority interests	**65**	–	**65**	–	–	–
Acquisitions	**76**	**93**	**169**	61	–	61
Increased stake in subsidiaries	**(40)**	–	**(40)**	–	–	–
Exchange movements	**(3)**	**(3)**	**(6)**	–	–	–
Profit and loss account	**12**	–	**12**	4	–	4
Closing minority interests	**110**	**90**	**200**	65	–	65

Non-equity minority interests include 100 per cent of the cumulative preferred stock of LGEC and 100 per cent of the cumulative preferred stock of KU, the regulated utility subsidiaries of LG&E. The majority of these preference shares are redeemable at 30 days' notice by each regulated utility subsidiary. Preference shareholders have first preference in the event of a liquidation of each utility subsidiary and first rights to dividends. The holders of these shares only have rights against the US utility subsidiaries.

28 Reconciliation of movements in shareholders' funds

	31 December 2000 £m	2 January 2000 £m	3 January 1999 £m
Profit/(Loss) for the financial period	**429**	708	(156)
Shares issued	**6**	4	30
Dividends	**(236)**	(226)	(157)
Currency translation differences on foreign currency net investments	**(32)**	63	(28)
Revaluation reserve arising on acquisition	–	25	–
Net increase/(decrease) in shareholders' funds for the period	**167**	574	(311)
Opening shareholders' funds	**1,919**	1,345	1,656
Closing shareholders' funds	**2,086**	1,919	1,345

Closing shareholders' funds include 49,998 limited-voting redeemable preference shares of £1 fully paid up.

29 Cash flow

a) Reconciliation of operating results to cash flow from operating activities:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Operating profit/(loss)	**483**	347	(153)
Depreciation (including exceptional items)	**292**	263	157
(Profit)/Loss on sale of tangible fixed assets	**(21)**	1	(33)
(Profit)/Loss on sale of investments	**(2)**	4	–
Goodwill amortisation	**75**	68	28
Decrease/(Increase) in stocks	**5**	(6)	13
(Increase)/Decrease in debtors	**(3)**	34	(124)
Increase/(Decrease) in creditors	**62**	(725)	528
(Decrease)/Increase in provisions	**(44)**	(13)	40
	847	(27)	456

The movement in creditors and provisions for the year ended 31 December 2000 includes cash outflows of £246 million (2 January 2000 £553 million, 3 January 1999 £12 million) relating to exceptional charges arising in previous years.

b) Analysis of changes in net debt in the year:

	31 December 2000 £m	Non-cash changes £m	Cash flow change £m	Acquisitions (excluding cash and overdrafts) £m	Exchange adjustments £m	2 January 2000 £m
Cash at bank and in hand	**137**	–	109	–	–	28
Overdrafts	**(3)**	–	34	–	–	(37)
	134	–	143	–	–	(9)
Debt due after one year	**(3,628)**	33	(325)	(814)	50	(2,572)
Debt due within one year: Short-term loans	**(2,300)**	(27)	(1,397)	(864)	49	(61)
Short-term deposits	**472**	–	(146)	–	–	618
	(5,322)	6	(1,725)	(1,678)	99	(2,024)

30 Financial instruments

Financial instruments and risk management

As part of the financing of its normal operating activities, the Group uses a variety of financial instruments. These may be assets, liabilities or related commitments, depending on requirements. These instruments are denominated in Sterling or foreign currencies and have various maturities and interest rates. The Group is exposed to movements in market interest rates and foreign currency exchange rates. Active steps are taken to manage these risks, both by management of the portfolio of financial instruments themselves, and by the use of derivative financial instruments, which are primarily used where there is an underlying exposure.

The objectives, policies and strategies connected with the use of financial instruments are discussed in the 'Treasury management' section of the Financial Review.

The Group may be exposed to credit related loss in the event of non-performance by counterparties under these instruments. However, the Group does not anticipate any non-performance given the high credit rating of the established banks and financial institutions that form these counterparties. The Group controls this credit risk through credit approvals, strict exposure limits, monitoring procedures and specific controls depending on the size of individual transactions. There are no significant concentrations of credit risk. The Group does not usually require collateral or other security to support financial instruments with credit risks.

Foreign exchange contracts and options

Powergen enters into foreign exchange contracts and options in accordance with its hedging policies. These policies are discussed under 'Foreign exchange risk management' in the Financial Review. The net Sterling amounts of each foreign currency Powergen has contracted to purchase (or sell), and has options to purchase are as follows:

	Foreign exchange contracts		Foreign exchange options	
	31 December 2000 Notional amount £m	2 January 2000 Notional amount £m	31 December 2000 Notional amount £m	2 January 2000 Notional amount £m
US Dollars	**119**	(31)	–	–
Portuguese escudos	–	(11)	–	–
Deutschmarks	–	14	–	–
Euros	**(139)**	(51)	–	–
Australian dollars	**(52)**	(62)	**(11)**	(12)
	(72)	(141)	**(11)**	(12)

Some contracts involve purchases or sales of USDollars against other, non-Sterling currencies. The Sterling equivalent amounts are as follows:

	31 December 2000 Notional amount £m	2 January 2000 Notional amount £m
Korean won	**(1)**	(18)
Euros	**(84)**	–
Indian rupees	**(35)**	–
	(120)	(18)

The weighted average time to maturity of foreign exchange contracts is two months (year ended 2 January 2000, four months).

Foreign currency swaps are entered into with the objective of stabilising the effect of exchange rate movements and effective Sterling interest rates applicable to debt. The notional amounts swapped to Sterling are as follows:

	31 December 2000 Notional amount £m	2 January 2000 Notional amount £m
Foreign currency swaps	**826**	864

There are no material monetary assets or liabilities of the Group that are not denominated in the functional currency of the entity concerned, other than certain non-Sterling borrowings treated as hedges of net investments in overseas operations.

Interest rate risk management

Powergen has a portfolio of fixed and floating interest rate debt and, in order to mitigate interest rate risk, arranges interest rate hedges to achieve a desired mix of fixed and floating interest rates, with a range of different maturities, as described in the Financial Review. The instruments used can be summarised as follows:

	31 December 2000 Notional amount £m	2 January 2000 Notional amount £m
Interest rate swap contracts	**1,023**	760

The weighted average time to maturity of interest rate swap contracts is 6.6 years (year ended 2 January 2000, 3.1 years).

In addition, there are interest rate swaptions with a notional principal amount of £1,674 million and fair value of £nil. These swaptions cap the interest payable on part of the USDollar term facility (see note 3).

Interest rate risk profile of financial assets and liabilities

			Fixed rate financial liabilities		
	Total	Floating rate financial liabilities		Weighted average interest rate	Weighted average period for which rate is fixed
At 31 December 2000	**£m**	£m	£m	%	Years
Sterling	**2,269**	1,468	801	8.6	10.8
US Dollar	**3,443**	2,946	497	7.1	9.8
Deutschmark	**190**	190	–	–	–
Indian rupee	**29**	29	–	–	–
	5,931	4,633	1,298	8.1	10.4

The figures in the above table are stated after taking account of relevant interest rate swap contracts.The swaptions then provide a fixed cap on £1,674 million of USDollar debt, resulting in the fixed/floating ratio complying with Board policy.

The floating rate financial liabilities bear interest at variable rates, in some cases fixed in advance for periods up to one year. The floating rates are determined with reference to the following rates:

Currency	Rate
Sterling	LIBOR
US Dollar	LIBOR, FIBOR, Bond Market Association Index
Deutschmark	LIBOR, FIBOR
Indian rupee	Banks' Prime Lending Rates

In addition to the above, the Group's provisions include £525 million (2 January 2000 £150 million) for contract provisions (see note 23) which meet the definition of financial liabilities. These financial liabilities are considered to be floating rate liabilities as, in establishing the provisions, the cash flows have been discounted. The discount rate is re-appraised at each reporting date to ensure that it reflects current market assessments of the time value of money and the risks specific to the liability.

At 31 December 2000, the Group held £442 million of financial assets in the form of Sterling bank deposits (2 January 2000 £646 million), £128 million in the form of US Dollar deposits (2 January 2000 £nil), and £39 million in other currencies (2 January 2000 £nil). These deposits earn interest at floating rates, fixed in advance for periods up to three months, by reference to Sterling LIBID and the 'iMoneyNet Government Institutional Average' for the Sterling and USDollar deposits respectively.

Fair value

The fair value of all these financial instruments, which reflects the estimated amounts Powergen would receive or pay to terminate the contracts at the year end based on market values, is shown below. The fair values therefore reflect current unrealised gains/(losses) on all open contracts.

	31 December 2000 Fair value £m	2 January 2000 Fair value £m
Foreign currency contracts	**(12)**	3
Foreign currency swaps	**13**	(49)
Interest rate swaps	**3**	(22)

The estimated fair values of the Group's financial assets and liabilities are as follows:

		31 December 2000		2 January 2000	
	Note	**Carrying amount £m**	**Fair value £m**	Carrying amount £m	Fair value £m
Assets:					
Cash and short-term deposits	1	**609**	**609**	646	646
Investments	2	**80**	**83**	70	71
Liabilities:					
Short-term debt	3	**(2,303)**	**(2,303)**	(98)	(98)
Long-term debt	4	**(3,628)**	**(3,580)**	(2,572)	(2,551)

1. The fair value of short-term deposits approximates tocarrying value due to the short maturity of instruments held.
2. The fair value of investments listed on a recognised stock exchange is estimated at quoted market price. Others are valued at cost.
3. The fair value of short-term debt approximates to the carrying value as the balance represents short-term loans and bank overdrafts.
4. The fair value of the long-term debt at the reporting date has been estimated at quoted market rates.

Short-term debtors and creditors are not included in these disclosures.

The movement in unrecognised gains and losses on instruments used for hedging is as follows:

	Gains £m	Losses £m	**Total net (losses)/gains £m**
Unrecognised gains/(losses) on hedges at 2 January 2000	10	(78)	(68)
(Gains)/Losses on hedges arising in previous periods that were recognised during the year	(6)	8	2
Gains/(Losses) on hedges arising before 2 January 2000 that were not recognised during the year	4	(70)	(66)
Gains/(Losses) on hedges arising during 2000 that were not recognised during the year	50	20	70
Unrecognised gains/(losses) on hedges at 31 December 2000	**54**	**(50)**	**4**
Of which:			
Gains/(Losses) expected to be recognised in 2001	6	(18)	(12)
Gains/(Losses) expected to be recognised in 2002 or later	48	(32)	16

The hedging of translation exposures associated with foreign currency net investments is however recognised in the balance sheet.

Contracts for differences

Given the variability of UK pool prices, Powergen's policy in the UK is to enter into Cfds which effectively fix the price of its expected output sold through the Pool. Powergen seeks to achieve a broad match between the cover provided by these contracts and its expected sales through the Pool, thereby removing the majority of exposure to movements in pool prices. Powergen's sales portfolio spans the entire electricity market and includes industrial, commercial and domestic customers.

Powergen has a variety of wholesale contract types of varying lengths (although generally of one year's duration), with a number of Regional Electricity Companies (RECs), under which Powergen believes the RECs hedge their purchases from the Pool to meet their customer electricity demand. These Cfd sales totalled 21 TWh for the year to 31 December 2000.

The majority of Powergen's Cfd contract cover for any particular year is secured between January and March.

Consequently the cover in place at the balance sheet date, for the twelve months to December 2001 equates to around 78 per cent of the Group's expected electricity output. The gross value of net Cfd sales cover outstanding as at 31 December 2000 was £53 million.

Any estimate of the fair value of the Cfds outstanding at the balance sheet date must necessarily be based on assumptions of a number of complex factors, including the level of long-term UK power prices, availability, bidding behaviour of others within the marketplace and the appropriate market discount rates. Based on management's estimates of future electricity prices, modelled under various scenarios, the fair value of the Cfd portfolio at 31 December 2000 is £22 million favourable.

These Cfds involve a degree of credit risk, being the risk that the counterparty to the Cfd defaults on settlement. The Group controls credit risk arising from holding the Cfds through credit approvals, limits and monitoring procedures.

31 Commitments and contingent liabilities

a) At 31 December 2000, the Group had commitments of £108 million (2 January 2000 £198 million) for capital expenditure, of which £5 million (2 January 2000 £18 million) related to expenditure to be incurred after one year.

b) The Group is aware of claims in respect of current and former employees, including former employees of the Central Electricity Generating Board, and contractors in respect of industrial illness and injury and other potential claims which involve or may involve legal proceedings against the Group. The directors are of the opinion, having regard to legal advice received, the Group's insurance arrangements and provisions held, that it is unlikely that the matters referred to above will, in aggregate, have a material effect on the Group's financial position, results of operations or liquidity.

c) The Group has in place a portfolio of fuel contracts of varying volume, duration and price, reflecting market conditions at the time of commitment. These contracts are with UK, US and other international suppliers of coal and are backed by transport contracts for rail, road, canal and sea movements. At 31 December 2000 the Group's future commitments for the supply of coal under all its contractual arrangements totalled £798 million.
The Group is also committed to purchase gas under various long-term gas supply contracts including the supply of gas to the Group's UK CCGT power stations. At 31 December 2000 the estimated minimum commitment for the supply of gas under all these contracts totalled £2,660 million.

d) In the normal course of business the Group gives certain other indemnities and guarantees which are not considered to be material in the context of these financial statements and on which no losses are anticipated to arise.

e) The Group has operating lease commitments for generating and other assets. The future minimum annual lease payments under these agreements are analysed as follows:

	At 31 December 2000 £m
2001	21
2002	21
2003	21
2004	21
2005	21
In more than five years	373
	478

32 Related party transactions

As part of its international activities the Group has contracted on an arms length basis to provide power station construction management and operation and maintenance services to certain associated companies. Total revenues during the year ended 31 December 2000 amounted to £12 million (year ended 2 January 2000 £13 million). There were no outstanding balances at either 31 December 2000 or 2 January 2000.

Prior to, and following, the net acquisition of 50 per cent of CPL on 29 September 2000 Powergen had a contract to purchase electricity output from CPL under a Cfd. The net difference payment for the nine months to September 2000 was £11 million to CPL and that for the year ended 31 December 2000 was £24 million (year ended 2 January 2000 £20 million). The balance outstanding at 31 December 2000 was a £5 million creditor (2 January 2000 £3 million creditor).

LG&E's Independent Power Operations division provides management, operation and accounting services to certain associated companies. Total revenues earned from providing these services amounted to £1 million for the 21 days ending 31 December 2000. The balance oustanding at 31 December 2000 was a £2 million debtor.

33 Post balance sheet events

On 21 February 2001, Powergen completed the sale of its East Midlands Electricity Metering Business to Siemens Metering Limited. At 31 December 2000, the approximate net asset value of the business being sold was £25 million.

On 27 February 2001, Powergen completed the sale of its Australian assets to companies which will be managed and 80 per cent owned by CLP Power International, a subsidiary of CLP Holdings Limited. Powergen will take a 20 per cent equity stake in these companies.

Summary of differences between UK and US generally accepted accounting principles

Powergen's consolidated financial statements have been prepared in accordance with UK GAAP which differs in certain significant respects from US GAAP. These differences relate principally to the following items, and the effect of the adjustments to net income and equity shareholders' funds which would be required under US GAAP are set out in the tables below.

a) **Pension costs and other post-employment benefits** Under UK GAAP, pension costs represent the expected cost of providing pension benefits to be charged to the profit and loss account so as to spread the cost over the expected average remaining service lives of employees. Under US GAAP, the annual pension cost comprises the estimated cost of benefits accruing in the period adjusted for any deficit or surplus arising at the time Statement of the United States Financial Accounting Standards Board (SFAS) 87 'Employers' Accounting for Pensions' was adopted. The charge is further adjusted to reflect the cost of benefit improvements and any surpluses/deficits which emerge as a result of the actuarial assumptions made not being borne out in practice. For US purposes, only those surpluses/deficits falling outside a 10 per cent fluctuation 'corridor' are being recognised.

b) **Severance costs** Under UK GAAP, voluntary severance costs for employees leaving as part of Powergen's on-going restructuring programme are accrued and recognised in the consolidated profit and loss account once the Group is demonstrably committed to such a programme and implementation has commenced. Voluntary severance costs include severance payments, payments in lieu of notice and the costs of providing incremental pension benefits in respect of staff reductions. Under US GAAP, voluntary termination benefits are generally charged in the year in which the employees accept the terms under which they will leave Powergen's employment. In addition, where the number of employees leaving results in a significant reduction in the accrual of pension benefits for employees' future service (a 'curtailment' under SFAS 88), the effects are reflected as part of the cost of such termination benefits.

c) **Capitalisation of interest** Under UK GAAP, Powergen capitalises interest payable where borrowings are specifically financing the construction of a major capital project with a long period of development. US GAAP requires that finance costs, which could theoretically have been avoided during construction of major capital projects, be included in tangible fixed assets and depreciated over the lives of the related assets. The amount of interest capitalised is determined by reference to average interest rates on outstanding long-term borrowings.

d) **Start-up costs** Under UK GAAP, start-up costs are expensed to the profit and loss account. Under US GAAP, prior to the effective date of US Statement of Position (SOP)98-5 'Reporting on the Costs of Start-Up Activities', it was acceptable to capitalise certain start-up costs on power station and similar energy projects. SOP 98-5 is effective for financial years commencing on or after 1 January 1999.

e) **Software** Under UK GAAP, capitalisation of the costs associated with internally developed software is not allowed. SOP 98-1 'Accounting for the Costs of Computer Software Developed or Obtained for Internal Use' requires capitalisation of the costs of internally developed software. These capitalised development costs are then depreciated over the useful life of the software.

f) **US regulatory assets and liabilities** Under US GAAP, SFAS 71 'Accounting for the Effects of Certain Types of Regulation' sets out the appropriate accounting treatment for US utilities whose regulators have the power to approve or regulate charges to customers. As long as through the regulatory process, the utility is substantially assured of recovering its allowable costs from, or is obligated to refund amounts to, customers, any costs/revenues not yet recovered, or refunded, may be deferred as regulatory assets/liabilities. Due to the different regulatory environment, no equivalent policy applies in the UK.

Under UK GAAP, Powergen's policy is to recognise regulatory assets/liabilities established in accordance with SFAS 71 only where they comprise rights or other access to future economic benefits which have arisen as a result of past transactions or events which have created an obligation to transfer economic benefits to a third party. Measurement of the past transaction or event and therefore the amount of the regulatory asset/liability, is determined in accordance with UK GAAP.

g) **Overhaul** Under UK GAAP, the costs associated with a major overhaul are capitalised as part of tangible fixed assets and amortised over the period to the next overhaul. Under US GAAP, the costs associated with major overhauls are generally recognised as these costs are incurred.

h) **Goodwill** Under UK GAAP and US GAAP, goodwill is held as an intangible asset in the balance sheet and amortised over its useful life. Under UKGAAP, prior to the adoption of Financial Reporting Standard (FRS) 10 'Goodwill and Intangible Assets' from 30 March 1998, goodwill arising was written off on acquisition against reserves.

i) **Investments** Under UK GAAP, investments in securities are accounted for at purchase cost with provision made for any impairment in value. Under US GAAP, SFAS 115 'Accounting for Certain Investments in Debt and Equity Securities' requires that certain investments in debt securities and equity securities are accounted for at fair value.

j) **Employee share option schemes** Under US GAAP, a compensation cost is recognised for the amount by which the quoted market value of the share at the date of grant exceeds the option price for compensatory plans as defined in APB 25. The cost is accrued over the approximate periods in which employees provide service to Powergen in consideration of the grant of options. Under UK GAAP, SAYE employee share option schemes are specifically exempt from the requirement to recognise any such compensation cost. There is no compensation cost associated with other employee share option schemes.

k) **Ordinary dividends** Under UK GAAP, ordinary dividends are provided for in the financial year in respect of which they are recommended by the Board of Directors for approval by shareholders. Under US GAAP, such dividends and tax are not provided for until the dividends are formally declared by the Board of Directors.

l) **Fixed asset impairment** Under UK GAAP, where an impairment loss has been recognised, the loss is reversed if the recoverable amount of the asset increases. US GAAP does not allow the reinstatement of previous fixed asset impairments.

m) **Deferred income** As described in note 3 to the financial statements, on 19 July 1999 Powergen completed the sale of Fiddler's Ferry and Ferrybridge C power stations to Edison Mission. As part of this transaction, Powergen is providing services under a major parts warranty in respect of each station, whereby, Powergen will have to pay certain amounts during each of the five years following the sale should the plant be unavailable during specified periods.

Summary of differences between UK and US generally accepted accounting principles continued

Under UK GAAP, amounts received in advance in respect of the provision of services under warranty arrangements are taken to deferred income and recognised in operating income over the period to which the warranty cover relates. Costs associated with the provision of services under warranty arrangements are included within operating costs when incurred. Under US GAAP, the Group is required to reserve for a reasonable estimate of the anticipated warranty expense. Direct costs incurred by the Group under the warranty arrangements will be used to reduce the reserve. The reserve will be examined and adjusted each year with movements being reflected in the Group's profit and loss account.

n) **Decommissioning costs** Under UK GAAP, a fixed asset and related provision is recognised in respect of the estimated total discounted cost of decommissioning generating assets. The resulting fixed asset is depreciated on a straight-line basis, and the discount on the provision is amortised over the useful life of the associated power stations. US GAAP requires that a charge is made annually against profits to accrue for the estimated cost of decommissioning major power plant.

o) **Deferred taxation** UK GAAP requires provision for deferred taxation only when it is expected that a liability will become payable or an asset will crystallise in the foreseeable future and then at the known future rates of tax. US GAAP requires full provision for deferred taxes to be made using enacted future tax rates.

p) **Cash flow statement** Under US GAAP, various items would be reclassified within the consolidated cash flow statement. In particular, interest received, interest paid (net of interest capitalised), interest on finance leases and taxation would form part of net cash flows from operating activities. Dividends paid would be included within net cash flows from financing. Net cash used in investing activities includes interest capitalised. Under US GAAP, all short-term debt (including commercial paper and bank overdrafts) would be included in financing activities.

q) **Earnings per share** Earnings per share computed in accordance with US GAAP has been based upon the following number of shares:

	31 December 2000	2 January 2000	3 January 1999
Weighted average shares in issue for UK and US GAAP basic earnings	**650,976,860**	649,552,248	646,681,662
Scrip dividends	–	–	1,474,315
Share options	**6,462,017**	3,281,183	3,732,182
Weighted average shares in issue for UK and US GAAP diluted earnings	**657,438,877**	652,833,431	651,888,159

r) **Extraordinary items** Under UK GAAP, income and expenses from non-recurring but significant transactions arising other than in the course of the Group's ordinary activities are recorded as exceptional items. Items classified as exceptional for purposes of UK GAAP generally do not meet the definition of 'extraordinary' under US GAAP and would be classified as operating expenses under US GAAP. However, costs and expenses resulting from debt extinguishments and exchanges of debt instruments with substantially different terms are classified as extraordinary under US GAAP.

s) **Comprehensive income** Under US GAAP, SFAS 130 'Reporting Comprehensive Income', requires disclosure of the components and total of comprehensive income for the period in which they are recognised in the financial statements. Comprehensive income is defined as the change in equity (net assets) of a business arising from transactions and other events and circumstances from non-owner sources. It includes all changes in shareholders' equity during the reporting period except those resulting from investments by owners and distributions to owners, including dividends. The disclosures required by SFAS 130 are substantially similar to those presented in the statement of total recognised gains and losses prepared under UKGAAP.

t) **US related costs** The GAAP difference for USrelated costs reflects the variation in timing of recognition of agreed payments made to senior executives as part of the acquisition of LG&E.

Effect on net income of differences between UK GAAP and US GAAP:

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Net income/(loss) under UK GAAP	**429**	708	(156)
US GAAP adjustments:			
Pension costs	**101**	48	49
Severance costs	**(7)**	(3)	(28)
Capitalised interest, net of related depreciation	**11**	7	1
US related costs	**13**	–	–
Goodwill amortisation	**(5)**	(5)	(3)
Share option scheme*	**(2)**	(1)	(1)
Fixed asset impairment	–	30	(30)
Deferred income	**(70)**	308	–
Decommissioning costs	**(1)**	(2)	–
Taxation effects on the foregoing adjustments	**(31)**	(36)	(7)
Deferred taxation	**(8)**	71	(9)
Net income/(loss) under US GAAP after extraordinary items	**430**	1,125	(184)
Less extraordinary items (net of taxation):			
Repayment of bonds (see note 3)	**32**	–	–
Net income/(loss) under US GAAP before extraordinary items	**462**	1,125	(184)
	pence	pence	pence
Basic earnings/(loss) per share under US GAAP after extraordinary items	**66.1**	173.2	(28.5)
Less: extraordinary items	**4.9**	–	–
Basic earnings/(loss) per share under US GAAP before extraordinary items	**71.0**	173.2	(28.5)
Diluted earnings/(loss) per share under US GAAP	**65.4**	172.3	(28.5)

* the movement on this adjustment is posted to reserves.

Effect on equity shareholders' funds of differences between UK GAAP and US GAAP:

	31 December 2000 £m	2 January 2000 £m
Equity shareholders' funds under UK GAAP	**2,086**	1,919
US GAAP adjustments:		
Pension costs	**252**	176
Severance costs	**1**	8
Capitalised interest, net of related depreciation	**93**	82
Start-up costs	**3**	–
Software costs	**19**	–
Regulatory assets and liabilities	**27**	–
Overhaul costs	**(20)**	–
US related costs	**13**	–
Goodwill	**364**	93
Investment*	**3**	2
Dividends	**166**	156
Deferred income	**238**	308
Decommissioning costs	**(37)**	(2)
Taxation effects on the foregoing adjustments	**(83)**	(85)
Deferred taxation	**(617)**	(344)
Equity shareholders' funds under US GAAP	**2,508**	2,313

* the movement on this adjustment is posted to reserves

Consolidated statement of cash flows

The table below summarises the consolidated cash flow statements as if presented in accordance with US GAAP, and includes the adjustment to reconcile cash and cash equivalents under US GAAP to cash under UK GAAP.

	Year ended 31 December 2000 £m	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m
Net cash provided by/(used in) operating activities	**630**	(150)	204
Net cash (used in)/provided by investing activities	**(2,134)**	901	(795)
Net cash provided by/(used in) financing activities	**1,467**	(186)	569
Net (decrease)/increase in cash and cash equivalents	**(37)**	565	(22)
Cash and cash equivalents under US GAAP at the beginning of the period	**639**	74	96
Cash and cash equivalents under US GAAP at the end of the period	**602**	639	74
Non-cash equivalent components of net debt under UK GAAP at the end of the period	**7**	7	19
Short-term debt at the end of the period	**(2,303)**	(98)	(88)
Long-term debt at the end of the period	**(3,628)**	(2,572)	(2,413)
Net debt under UK GAAP at the end of the period	**(5,322)**	(2,024)	(2,408)

There were no significant non-cash investing or financing activities during the year.

Cash and cash equivalents

US GAAP defines cash and cash equivalents as deposits with banks and financial institutions that are unrestricted as to withdrawal or use, and which have original maturities of three months or less.

Five Year Summary

Summarised Profit and Loss Accounts	**Year ended 31 December 2000 £m**	Year ended 2 January 2000 £m	Nine months ended 3 January 1999 £m	Year ended 29 March 1998 £m	Year ended 30 March 1997 £m
Group turnover	**4,191**	3,746	2,344	2,932	2,898
Group operating profit before exceptionals	**580**	640	382	589	592
Net income/(loss) from interests in associated undertakings and joint ventures	**13**	28	14	5	(19)
Exceptional items	**26**	250	(537)	(369)	2
Net interest payable – Group	**(151)**	(156)	(104)	(15)	(7)
Profit/(Loss) before taxation	**468**	762	(245)	210	568
Taxation, including windfall tax	**(27)**	(50)	89	(335)	(148)
Profit/(Loss) after taxation	**441**	712	(156)	(125)	420
Minority interest	**(12)**	(4)	–	–	5
Profit attributable to shareholders	**429**	708	(156)	(125)	425
Dividends	**(236)**	(226)	(157)	(189)	(160)
Retained profit/(loss) for the year (6)	**193**	482	(313)	(314)	265
Earnings per ordinary share (pence) (1) (2) (3) (4) (5) (6)	**66.7**	73.4	38.8	68.1	63.0
Dividends per ordinary share (pence)	**36.2**	34.8	24.1	29.0	25.2
Dividend per ADS (£)	**1.45**	1.39	0.96	1.16	1.01
Amounts in accordance with US GAAP:					
Net income/(loss) for the year (7)	**432**	1,125	(184)	44	481
Basic earnings/(loss) per ADS (£) (7)	**2.64**	6.93	(1.14)	0.27	2.86
Diluted earnings/(loss) per ADS (£) (7)	**2.62**	6.89	(1.14)	0.27	2.83

Summarised Consolidated Balance Sheets	**31 December 2000 £m**	2 January 2000 £m	3 January 1999 £m	29 March 1998 £m	30 March 1997 £m
Fixed assets	**9,191**	5,011	4,937	2,676	3,142
Stocks	**258**	127	173	178	170
Debtors	**1,034**	733	760	515	486
Creditors and provisions	**(2,875)**	(1,863)	(2,117)	(1,232)	(1,121)
	7,608	4,008	3,753	2,137	2,677
Short-term borrowings	**(2,303)**	(98)	(88)	(10)	(132)
Long-term loans	**(3,628)**	(2,572)	(2,413)	(586)	(585)
Short-term deposits	**609**	646	93	115	62
Net borrowings	**(5,322)**	(2,024)	(2,408)	(481)	(655)
Total net assets	**2,286**	1,984	1,345	1,656	2,022
Minority interests	**(200)**	(65)	–	–	–
Shareholders' funds (6)	**2,086**	1,919	1,345	1,656	2,022
Share capital and share premium	**335**	329	325	392	365
Shares in issue (millions)	**651.5**	649.7	649.1	644.5	637.4
Amounts in accordance with US GAAP:					
Shareholders' funds	**2,510**	2,313	1,265	1,632	1,813
Total assets	**11,583**	6,664	6,101	3,493	3,886
Total long-term liabilities	**4,892**	3,493	3,275	1,112	1,313

Notes

(1) In the year ended 31 December 2000, earnings per ordinary share is based on profit before goodwill amortisation and exceptional items and after taxation and minority interests for the financial year of £434 million. Including exceptional items and after goodwill amortisation, earnings per ordinary share was 65.9 pence.

(2) In the year ended 2 January 2000, earnings per ordinary share is based on profit before goodwill amortisation and exceptional items and after taxation and minority interests for the financial year of £477 million. Including exceptional items and after goodwill amortisation, earnings per ordinary share was 109.0 pence.

(3) In the nine months ended 3 January 1999, earnings per ordinary share is based on profit before goodwill amortisation and exceptional items and after taxation for the financial period of £251 million. Including exceptional items and after goodwill amortisation, loss per ordinary share was 24.1 pence.

(4) In the year ended 29 March 1998, earnings per ordinary share is based on profit before exceptional items and after taxation for the financial year of £437 million. Including exceptional items, loss per ordinary share was 19.5 pence.

(5) In the year ended 30 March 1997, earnings per ordinary share is based on profit before exceptional items and after taxation and minority interests for the financial year of £423 million. Including exceptional items, earnings per ordinary share was 63.3 pence.

(6) Retained profit/(loss) for the year, earnings per share and shareholders' funds for the two years ended March 1998 were restated following the adoption of Financial Reporting Standard 12 from 30 March 1998.

(7) The net income/(loss) is equal to the net income/(loss) from continuing operations in all financial periods.

Shareholder Information

Shareholder Profile

as at 24 February 2001

	No. of holders	% of total holders	No. of ordinary shares	% of issued capital
1– 250	552,419	79.06	73,060,537	11.21
251– 750	123,540	17.68	48,727,520	7.48
751– 1,000	8,609	1.23	7,600,364	1.17
1,001– 10,000	12,991	1.86	29,298,755	4.50
10,001– 30,000	495	0.07	8,205,537	1.26
30,001– 100,000	308	0.04	18,441,704	2.83
100,001– 500,000	244	0.03	58,913,200	9.04
500,001–1,000,000	67	0.01	46,723,333	7.17
1,000,001 and above	72	0.01	360,707,519	55.35
	698,745	100	651,678,469	100

Financial Calendar

The Company will now be announcing results and paying dividends on a quarterly basis. In addition, from the first quarter onwards the US $ dividend rate to be paid on the ADRs will be set at the time of the relevant announcement of results, and paid on the same day as the UKdividend.

The Financial Calendar for 2001 is as follows:

	Preliminary Results	Q1 results	Q2 results	Q3 results
Announcement Date	21 Feb	3 May	2 Aug	1 Nov
Ex Dividend Date	28 Feb	16 May	8 Aug	7 Nov
Record Date	2 Mar	18 May	10 Aug	9 Nov
Payment Date	30 Mar	15 Jun	14 Sep	14 Dec

The Company's Annual General Meeting will be on Tuesday 1 May 2001, commencing at 11.00 am at The ICC, Birmingham.

Dividend Re-Investment Plan (DRIP)

Powergen is offering a Dividend Re-Investment Plan (DRIP) to shareholders, operated by our Registrars, Computershare Services PLC. Full details of the Plan, which uses shareholders' dividends to purchase extra shares to be added to their holdings, may be obtained from the Registrars at the address below under 'Shareholder Enquiries'. A small commission will be charged for the service.

Company Nominee Service

Powergen offers a Company Nominee Service, which is likely to be of most interest to private investors who deal frequently in the Company's shares – say more than twice a year.

The key features of the Company Nominee Service are:

- shares are held in a nominee account, and regular statements of account are provided, rather than share certificates;
- it provides a facility to allow shareholders to deal in Powergen shares rapidly and cost effectively through the CREST electronic settlement system;
- the benefits of direct shareholding are retained, such as prompt payment of dividends, a copy of the Annual Review, and attendance and voting at the Annual General Meeting;
- the Nominee Service is provided at no cost to the shareholder. However, if the facility to deal in Powergen shares is used, charges are payable. Basic commission is 1 per cent with a £10 minimum charge.
  Full details of the Company Nominee Service may be obtained from the Registrar at the address shown below under 'Shareholder Enquiries'.

Low Cost Share Dealing Service

A simple and economic way of buying or selling certificated shareholdings is still available through Hoare Govett. This is a postal dealing service, with a basic 1 per cent commission subject to a minimum charge of £10. Full details may be obtained from Pershing Securities on 020 7661 6616 (Purchases) or 020 7661 6617 (Sales).

Shareholder Information continued

Dividend History

To assist shareholders with the completion of their tax returns, a dividend history is set out below:

Payment	Date	Net amount per share	Scrip: Price of New Share Results
1	21 Oct 1991	5.55p	–
2	27 Mar 1992	3.05p	–
3	19 Oct 1992	6.20p	261.0p
4	26 Mar 1993	3.35p	294.2p
5	31 Mar 1993	7.15p	–
6	12 Nov 1993	3.95p	417.0p
7	29 Jul 1994	8.70p	465.6p
8	20 Dec 1994	5.00p	550.6p
9	28 Jul 1995	10.00p	498.0p
10	20 Dec 1995	6.50p	531.8p
11	31 Jul 1996	14.50p	485.0p
12	20 Dec 1996	7.80p	579.1p
13	31 Jul 1997	17.40p	658.5p
14	31 Dec 1997	9.00p	781.6p
15	31 Jul 1998	20.00p	776.8p
16	8 Dec 1998	10.00p	–
17	13 May 1999	14.10p	–
18	29 October 1999	10.80p	–
19	10 May 2000	24.00p	–
20	3 November 2000	10.80p	–

Capital Gains Tax: The price paid for the Company's Ordinary share at certain key events is listed below:

Event	Date	Price paid per share
Flotation: First Instalment	12 March 1991	100p
Flotation: Second Instalment *	4 February 1992	75p
40% Sale: First Instalment	6 March 1995	185p
40% Sale: Second Instalment *	6 February 1996	185p
40% Sale: Third Instalment *	17 September 1996	142p

* An instalment discount incentive was available under both offers, which offered a reduction on the instalments shown to shareholders who elected for that incentive.

The market price of the Company's Ordinary share on the issue of the bonus shares was:

Event	Date	Price paid per share
Flotation: Bonus Shares	31 March 1994	538.5p
40% Sale: Bonus Shares	31 March 1998	835.5p

Enquiries

• On your shareholding

Enquiries on your shareholding can be made using the link to the Registrars from the Company's website **www.powergenplc.com.** Shareholders will need their Shareholder Reference Number (SRN) which appears on the Proxy Form and other communications from the Company.

Alternatively enquiries may be made to the Registrar at the following address:
Computershare Services PLC, PO Box 96, The Pavilions, Bridgwater Road, Bristol BS99 7ZG.
Telephone: 0870 702 0103 (Calls charged at National Rate)
Fax: 0870 703 6119

• On the company

General information about the Company can be seen on the website at **www.powergenplc.com**

You may e-mail the Company Secretary on david.jackson@pgen.com
Alternatively you may contact him at:
Powergen plc, 53 New Broad Street, London EC2M 1SL
Telephone: 020 7826 2826
Fax: 020 7826 2890

• On ADR holdings

Enquiries on ADR holdings should be made to the Depositary for American Depositary Receipts at www.adrbny.com
Alternatively, you may contact The Bank of New York, Attention ADR Department, 101 Barclay Street, New York, NY 10286, USA
Telephone: (800) 524 4458 toll free.

Unsolicited Mail

The Share Register is a public document under the law, and some shareholders may have received unsolicited mail from other organisations taking advantage of this situation. If you wish to limit the amount of such mail, please write to the Mailing Preference Service, FREEPOST 22, London W1E 7EZ. You may still however receive mail from organisations which do not subscribe to this service.

Telephone information service

For a short commentary on Powergen's business together with the latest share price, telephone 0839 505900 (calls charged at 50p/min at all times, including VAT).

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