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BIRTH OF A WORLD LEADER

Valencia, April 26th 2007

Technical Session IV

ScottishPower
UK Regulated businesses:
Transmission &
Distribution

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Legal Note

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Key messages

- Value creation based on regulatory out-performance of allowances and incentive targets
- Attractive, increasingly incentive based, RPI-X regulatory framework
- Clear value creation potential for distribution (opex) and transmission (capex)
- Attractive asset mix
  - English and Scottish Distribution
  - Scottish Transmission

Agenda

Market overview

a. General
b. Transmission
c. Distribution

ScottishPower – T&D

Ofgem regulates the UK electricity and gas markets …

Ofgem is the regulator of the Gas and Electricity Markets Authority. Northern Ireland's Regulator is Ofreg

Cost of transmission and distribution: 25-30% of average domestic electricity bill

Ofgem protects consumers by promoting competition and ensuring effective regulation of "wires and gas pipes"

Regulation of the "wires" businesses has lead to cost reductions and has been successful

Regulation based on price cap (RPI-X) methodology

… through a price-setting mechanism …

Five year price control period

Operator base revenue allowances linked to revenue driver – equally weighted function of units distributed and number of customers

Regulatory revenue also linked to incentive mechanisms, for example relating to Losses and Quality of Service

Pass-through for costs of business rates on network assets, licence fees, transmission charges and other specified non-controllable costs

Correction mechanism adjusts price control for previous over/under recovery of revenue

Current distribution price control mechanism (2005-2010) will be in place until 2010 and transmission until 2012

… that allows generation of minimum returns

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Business activity	2008 WACC real post tax
Electricity distribution	4.80%
Electricity transmission (Scotland, England & Wales)	4.40%
Gas distribution	4.38%
Gas transmission	4.40%
Water and sewerage	5.10%

In the UK the price setting mechanism allows T&D companies to earn regulated target returns on their investment

Source: Ofgem

Price-setting mechanism – example

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Example (5 year)	REGULATION	
Allowed revenue	Eur 500 MM	This is fixed subject to incentives
Allowed opex	Eur 208 MM	Beat the opex target
Allowed capex / dep	Eur 150 MM	Beat the capex target
Allowed return (pre tax)	Eur 138 MM 6.9%	Increased realised return

RAB
Eur 2,000 MM

Although revenue requirement is fixed by Ofgem, the return can be improved by beating opex and capex / depreciation allowances

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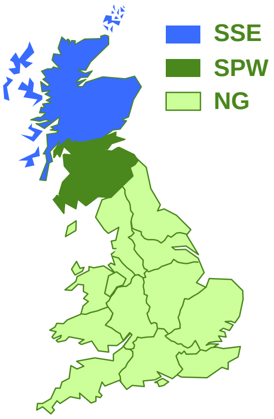
UK transmission network split between National Grid, Scottish & Southern and ScottishPower …

Description

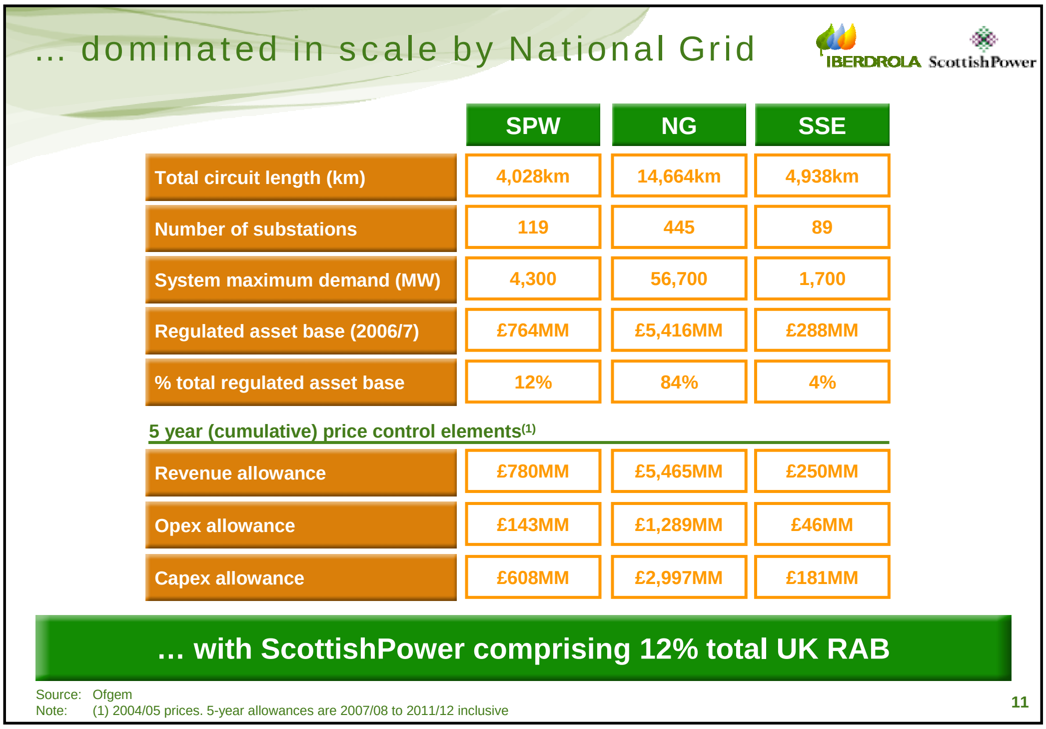
- In England and Wales, National Grid (“NG”) is the owner of the single transmission network (excluding 132kV network)
- In Scotland, ScottishPower and Scottish and Southern Energy own two separate transmission networks, and are responsible for planning, constructing and maintaining the network (including 132kV network)
- NG is the system operator for the whole GB region (under BETTA)
- NG’s subsidiary, Elexon, manages the governance and settlement of trading arrangements

UK geographic coverage



ScottishPower is one of three transmission network owners in the UK

Source: Ofgem, company web sites and annual reports



… dominated in scale by National Grid

	SPW	NG	SSE
Total circuit length (km)	4,028km	14,664km	4,938km
Number of substations	119	445	89
System maximum demand (MW)	4,300	56,700	1,700
Regulated asset base (2006/7)	£764MM	£5,416MM	£288MM
% total regulated asset base	12%	84%	4%
5 year (cumulative) price control elements(1)			
Revenue allowance	£780MM	£5,465MM	£250MM
Opex allowance	£143MM	£1,289MM	£46MM
Capex allowance	£608MM	£2,997MM	£181MM

… with ScottishPower comprising 12% total UK RAB

Source: Ofgem
Note: (1) 2004/05 prices. 5-year allowances are 2007/08 to 2011/12 inclusive

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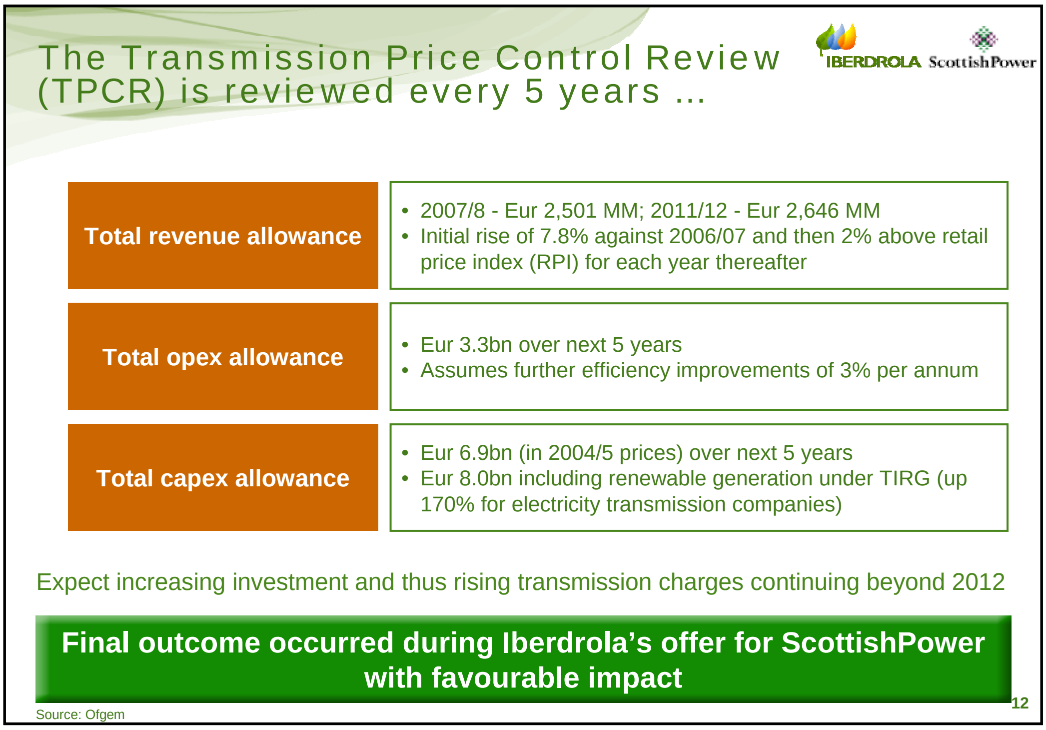


The Transmission Price Control Review (TPCR) is reviewed every 5 years …

Total revenue allowance	• 2007/8 - Eur 2,501 MM; 2011/12 - Eur 2,646 MM • Initial rise of 7.8% against 2006/07 and then 2% above retail price index (RPI) for each year thereafter
Total opex allowance	• Eur 3.3bn over next 5 years • Assumes further efficiency improvements of 3% per annum
Total capex allowance	• Eur 6.9bn (in 2004/5 prices) over next 5 years • Eur 8.0bn including renewable generation under TIRG (up 170% for electricity transmission companies)

Expect increasing investment and thus rising transmission charges continuing beyond 2012

Final outcome occurred during Iberdrola's offer for ScottishPower with favourable impact

Source: Ofgem

… and provides scheduling, balancing as well as some other mandatory and

Real time Balancing Services

- Generators schedule plants
- Generators inform NG of expected levels
- NG balances one hour prior to start by:
  - trading in the forward market when generation insufficient or excessive
  - accepting bids and offers from generators and consumers
  - using ancillary services contracts, negotiated in advance
- NG recovers cost through the Balancing Services Use of System charge (BSUOS)
  - based on costs incurred per half hour
  - pro-rated by generation and consumption volumes during that period

Ancillary services

- Mandatory services
  - Reactive power
  - Frequency response
- Black start and Fast start
- Commercial services
  - Maximum Generation Service
  - Enhanced Reactive Service
  - Commercial Frequency Response
  - Fast Reserve
  - Standing Reserve
  - Warming
  - Emergency Assistance
- Other services

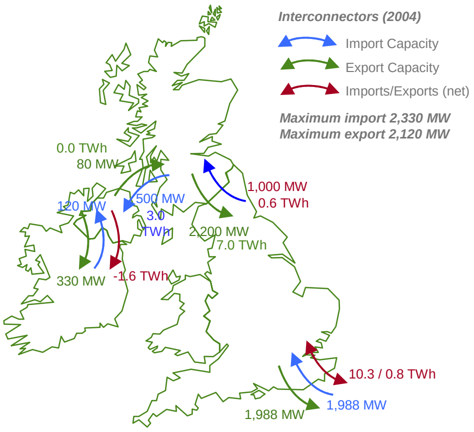
NG provides real time balancing services and ancillary services apart from being the largest transmission network owner in the UK

Interconnection

Description

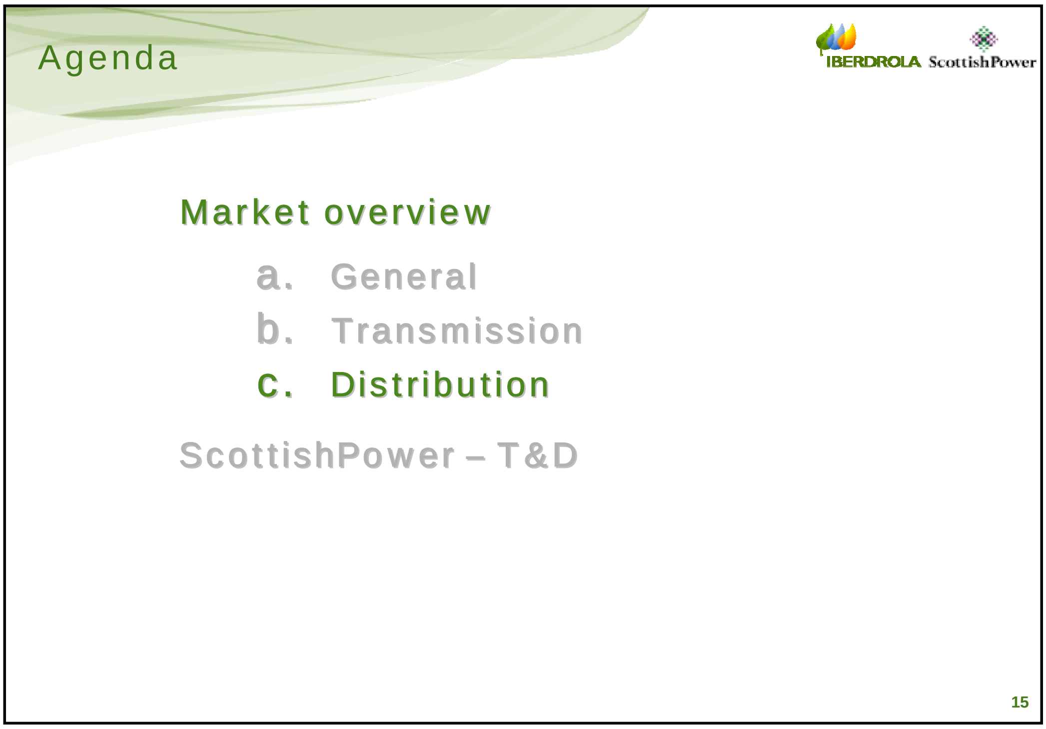
- Main transmission flows are north to south
- Interconnection with Scotland limited at c.2,200 MW
  - key for further renewables development in Scotland
  - upgrade of interconnector to 2,800 MW by 2010 underway
  - funding for increase to 3,200 MW by 2012 agreed with Ofgem
- 2002: new 500 MW interconnector between Scotland and Northern Ireland was commissioned

UK geographic coverage



Further plans for interconnection with the Netherlands and Norway of c.800 MW each

Source: CERA



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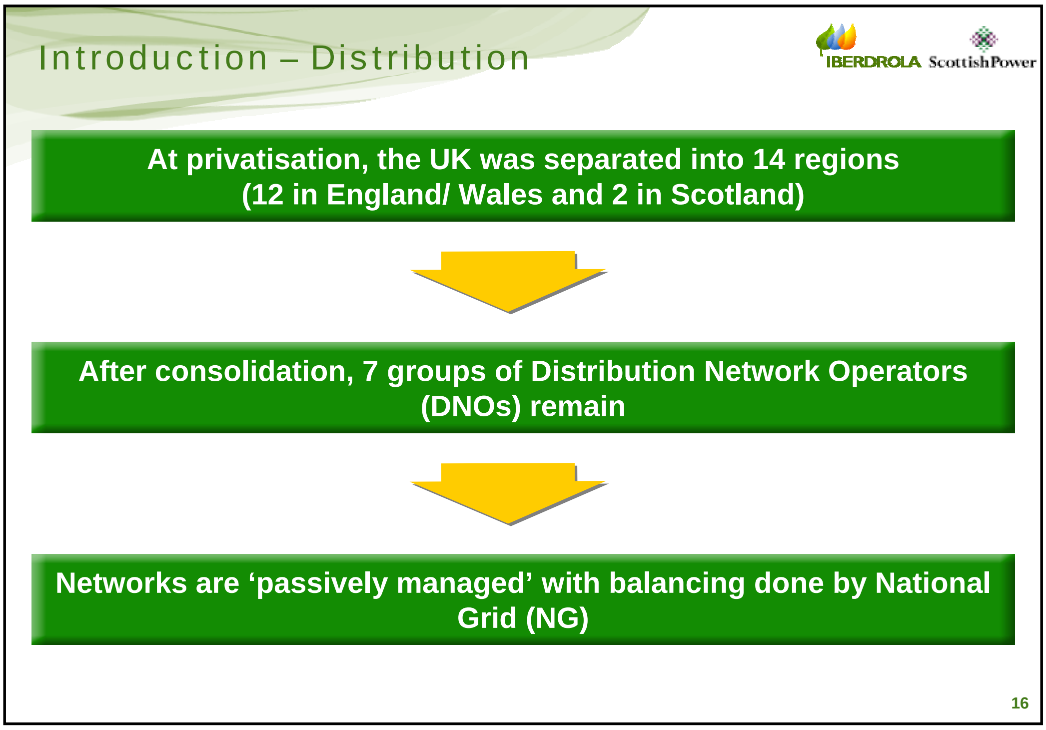
b. Transmission
c. **Distribution**

ScottishPower – T&D

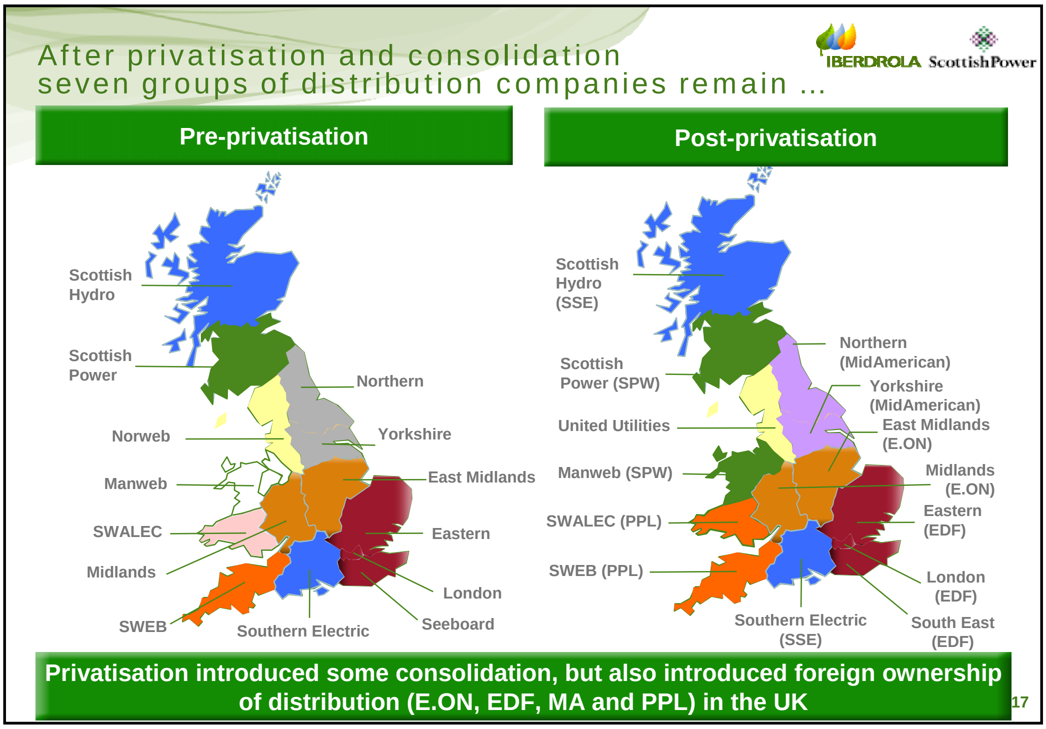


Introduction – Distribution

At privatisation, the UK was separated into 14 regions (12 in England/ Wales and 2 in Scotland)

After consolidation, 7 groups of Distribution Network Operators (DNOs) remain

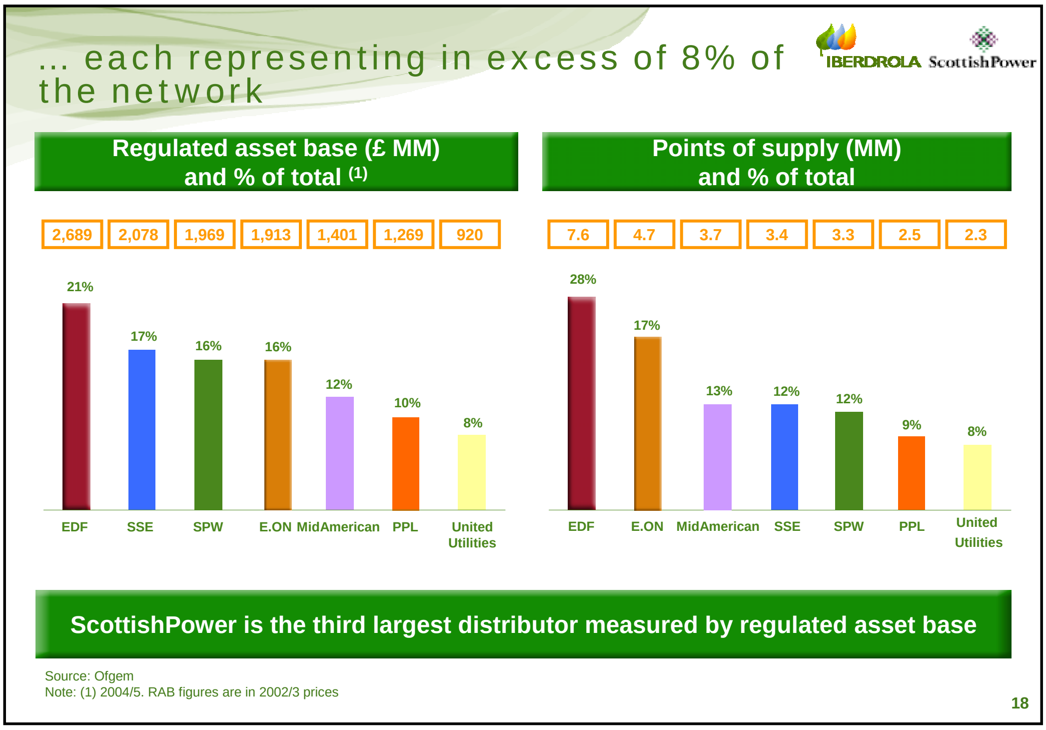
Networks are ‘passively managed’ with balancing done by National Grid (NG)



After privatisation and consolidation seven groups of distribution companies remain …

Pre-privatisation | **Post-privatisation**

Privatisation introduced some consolidation, but also introduced foreign ownership of distribution (E.ON, EDF, MA and PPL) in the UK



… each representing in excess of 8% of the network

Regulated asset base (£ MM) and % of total (1)

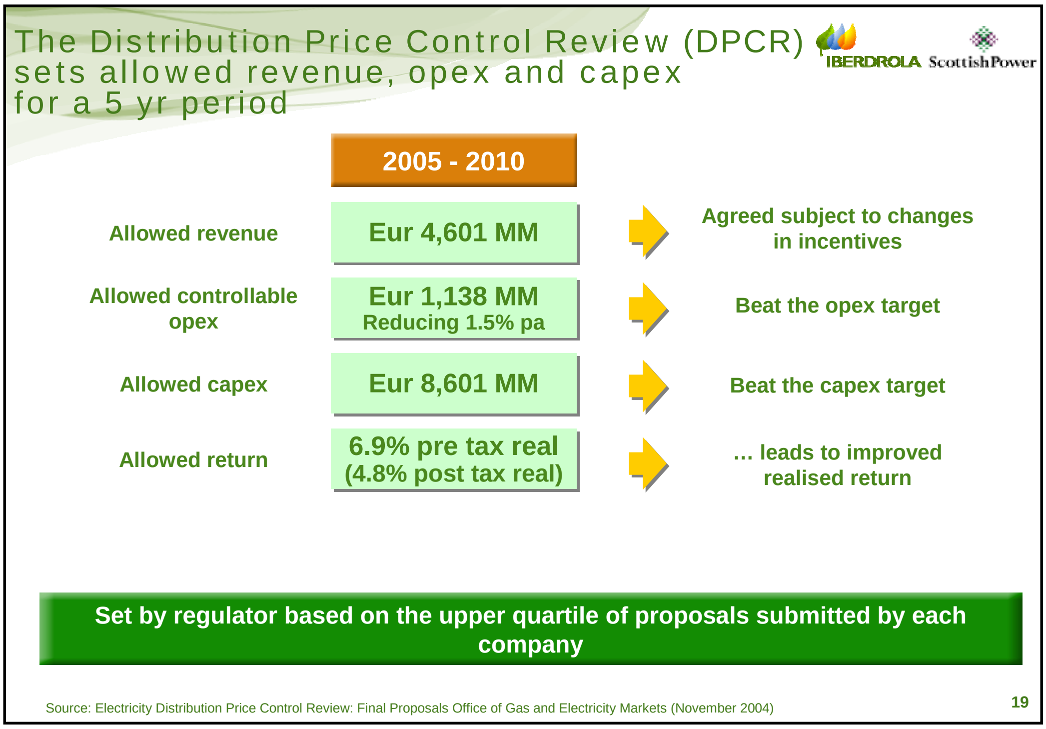
EDF	2,689	21%
SSE	2,078	17%
SPW	1,969	16%
E.ON	1,913	16%
MidAmerican	1,401	12%
PPL	1,269	10%
United Utilities	920	8%

Points of supply (MM) and % of total

EDF	7.6	28%
E.ON	4.7	17%
MidAmerican	3.7	13%
SSE	3.4	12%
SPW	3.3	12%
PPL	2.5	9%
United Utilities	2.3	8%

ScottishPower is the third largest distributor measured by regulated asset base

Source: Ofgem
Note: (1) 2004/5. RAB figures are in 2002/3 prices



The Distribution Price Control Review (DPCR) sets allowed revenue, opex and capex for a 5 yr period

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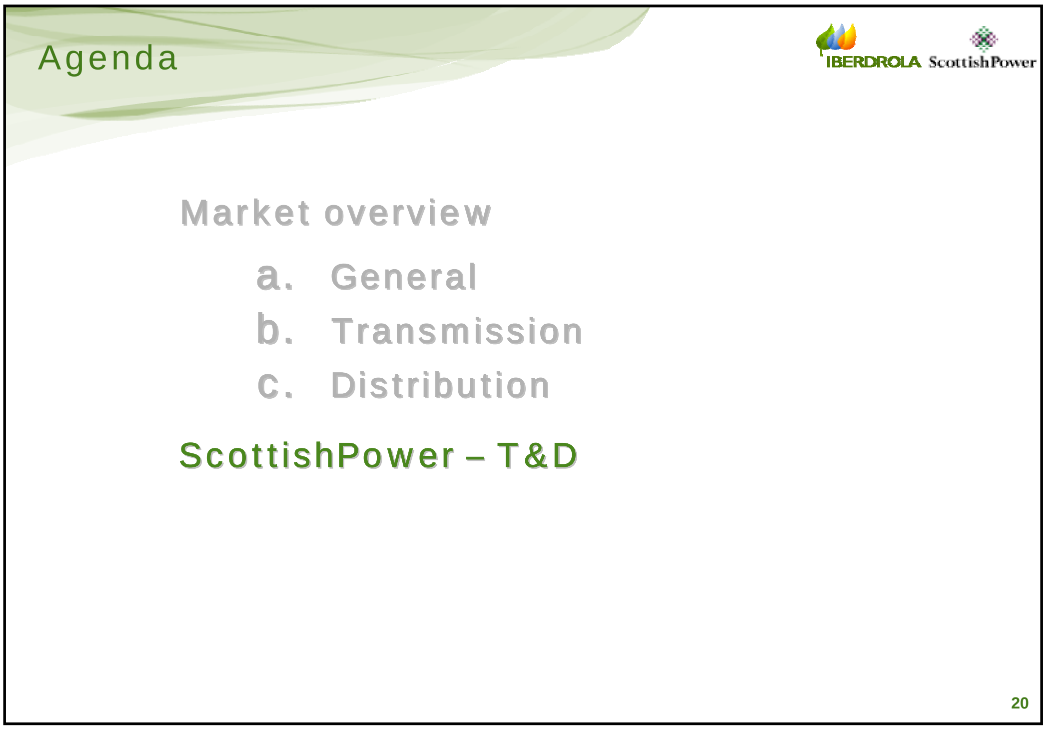
	2005 - 2010		
Allowed revenue	Eur 4,601 MM	➔	Agreed subject to changes in incentives
Allowed controllable opex	Eur 1,138 MM Reducing 1.5% pa	➔	Beat the opex target
Allowed capex	Eur 8,601 MM	➔	Beat the capex target
Allowed return	6.9% pre tax real (4.8% post tax real)	➔	… leads to improved realised return

Set by regulator based on the upper quartile of proposals submitted by each company

Source: Electricity Distribution Price Control Review: Final Proposals Office of Gas and Electricity Markets (November 2004)



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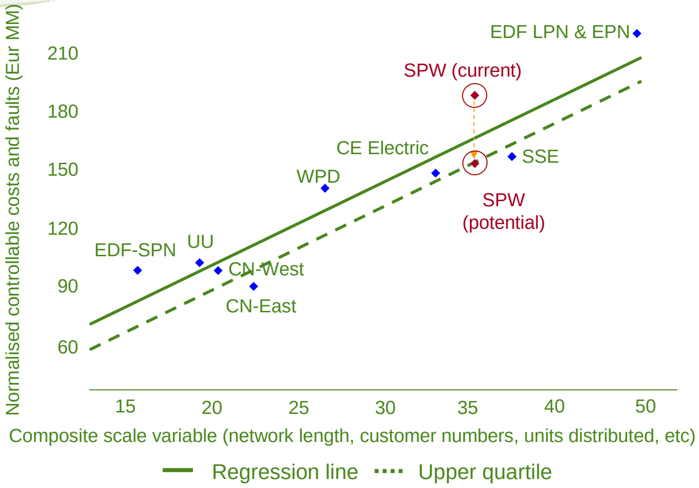
ScottishPower – T&D

Different players have varying degrees of success …

Based on Ofgem's cost efficiency analysis ScottishPower is less efficient than a number of its peers taking size, network length, customers, etc into consideration



Relative to peers ScottishPower has significant scope for cost reduction which leaves room for higher returns

Source: Ofgem, Distribution Price Control Review, Final Proposals

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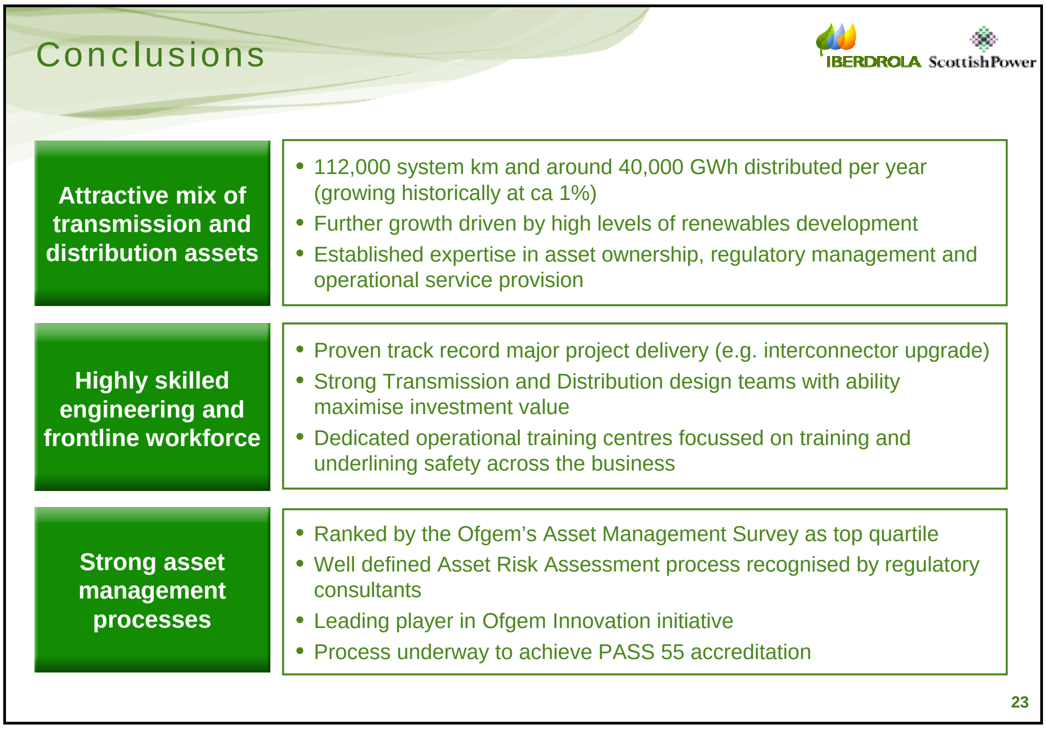
… with ScottishPower offering cost improvements

	Allowed	Levers to deliver improvement	
Revenue	**Eur 733MM**	• Programme of network automation	*Striving for improved performance*
Opex (1)	**Eur 208MM**	• Mobile information technology • Satellite navigation • Network control centre at Kirkintilloch	*Improved operating practices*
Capex	**Eur 286MM**	• Innovative design • Smart procurement	*Continuous drive for capital efficiencies*
Return	**6.9%** **Annual average for 5 years**	**Ongoing dialogue with Ofgem to ensure allowed returns encourage continued investment in the networks**	

Room for improvement in network performance

Note: (1) Opex includes allocation of corporate costs



Conclusions

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Attractive mix of transmission and distribution assets

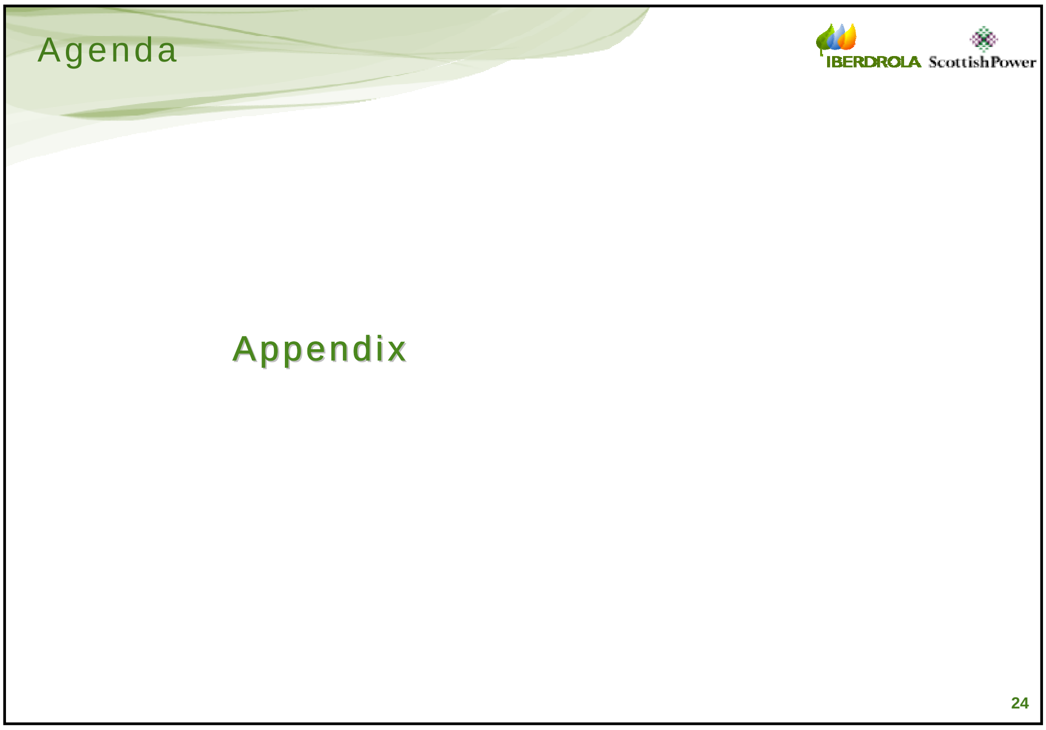
- 112,000 system km and around 40,000 GWh distributed per year (growing historically at ca 1%)
- Further growth driven by high levels of renewables development
- Established expertise in asset ownership, regulatory management and operational service provision

Highly skilled engineering and frontline workforce

- Proven track record major project delivery (e.g. interconnector upgrade)
- Strong Transmission and Distribution design teams with ability maximise investment value
- Dedicated operational training centres focussed on training and underlining safety across the business

Strong asset management processes

- Ranked by the Ofgem's Asset Management Survey as top quartile
- Well defined Asset Risk Assessment process recognised by regulatory consultants
- Leading player in Ofgem Innovation initiative
- Process underway to achieve PASS 55 accreditation



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Appendix

UK electricity distributors: key figures

	EDF	SSE	SPW	E.ON	MA	PPL	UU
Network length ('000km)	172	122	113	129	91	82	59
Points of supply (MM)	7.6	3.4	3.3	4.7	3.7	2.5	2.3
% total points of supply	28%	12%	12%	17%	13%	9%	8%
Units distributed (GWh)	84.5	41.3	39.1	56.2	41.3	28.0	25.4
Minutes lost per cust.	67 min	76 min	68 min	92 min	69 min	56 min	57 min
Reg. asset base (04/05)	£2,689MM	£2,078MM	£1,969MM	£1,913MM	£1,401MM	£1,269MM	£920MM
% total asset base	21%	17%	16%	16%	12%	10%	8%
5 year (cumulative) price control elements[1]							
Revenue allowance	£3,488MM	£2,562MM	£2,352MM	£2,466MM	£1,826MM	£1,644MM	£1,149MM
Opex allowance[2]	£1,642MM	£1,239MM	£991MM	£1,154MM	£898MM	£817MM	£526MM
Capex allowance[2]	£1,789MM	£858MM	£859MM	£1,101MM	£724MM	£537MM	£513MM

ScottishPower is the third largest distributor measured by regulated asset base

Source: Ofgem

[1] 2002/03 prices. 5-year allowances are 2005/06 to 2009/10 inclusive

[2] Capex excludes entire pension cost allowance; Opex includes entire pension cost allowance, tax and incentives

End of Technical Session IV

ScottishPower
UK Regulated businesses: Transmission & Distribution