

**THIS CIRCULAR AND ANY ACCOMPANYING DOCUMENTS ARE IMPORTANT AND REQUIRE YOUR IMMEDIATE ATTENTION.** If you are in any doubt as to the action you should take, you are recommended to seek your own independent financial advice from your stockbroker, bank manager, solicitor, accountant or other independent financial adviser authorised under the Financial Services and Markets Act 2000 if you are resident in the United Kingdom or, if not, from another appropriately authorised independent financial adviser.

If you have sold or transferred all of your holding of Ordinary Shares in Drax Group plc, please forward this Circular and the accompanying documents (but not the personalised Form of Proxy or Form of Direction), as soon as possible, to the purchaser or the transferee or to the person through whom the sale or transfer was effected for transmission to the purchaser or the transferee.

Any person (including, without limitation, custodians, nominees and trustees) who may have a contractual or legal obligation or may otherwise intend to forward this Circular to any jurisdiction outside the United Kingdom should seek appropriate advice before taking any action. The distribution of this Circular and any accompanying documents into jurisdictions other than the United Kingdom may be restricted by law. Any person not in the United Kingdom into whose possession this Circular and any accompanying documents come should inform themselves about and observe any such restrictions. Any failure to comply with these restrictions may constitute a violation of the securities laws of any such jurisdiction.

**You should read the whole of this Circular and all documents incorporated into it by reference in their entirety. Your attention is drawn to the letter from Philip Cox CBE, the Chairman of Drax Group plc, which is set out in Part I of this Circular and which contains a unanimous recommendation from the Board of Drax Group plc that you vote in favour of the Resolution to be proposed at the General Meeting referred to below. Part II of this Circular entitled “Risk Factors” includes a discussion of certain risk factors which should be taken into account when considering the matters referred to in this Circular.**



**Drax Group plc**

*(Registered in England and Wales with registered number 5562053)*

**Proposed acquisition by Drax Group plc of ScottishPower Generation Limited  
and  
Notice of General Meeting**

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A notice convening a General Meeting of Drax Group plc to be held at the offices of FTI Consulting, 200 Aldersgate Street, London EC1A 4HD on 21 December 2018 at 10.00am is set out at the end of this Circular.

For Shareholders, a Form of Proxy for use at the General Meeting is enclosed with this Circular. Whether or not you propose to attend the General Meeting, you are requested to complete and submit a Form of Proxy to the Company's Registrars, Equiniti Limited, Proxy Department, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA to arrive by no later than 10.00am on 19 December 2018.

If you hold shares in CREST, you may appoint a proxy by completing and transmitting a CREST Proxy Instruction to Equiniti Limited (CREST participant ID RA19) so that it is received by no later than 10.00am on 19 December 2018.

The return of a completed Form of Proxy or CREST Proxy Instruction will not prevent you from attending the General Meeting and voting in person if you wish to do so.

For Share Incentive Plan participants, a Form of Direction is enclosed with this Circular and, if used, should be sent to the trustee, Equiniti Share Plan Trustee Limited at Aspect House, Spencer Road,

Lancing, West Sussex BN99 6DA, to arrive by no later than 10.00am on 17 December 2018. As a participant in the Share Incentive Plan you are unable to attend the General Meeting unless you hold shares registered in your own name.

This document is a circular relating to the Acquisition which has been prepared in accordance with the Listing Rules and approved by the Financial Conduct Authority.

No person has been authorised to give any information or make any representations other than those contained in this Circular and, if given or made, such information or representations must not be relied on as having been so authorised. The delivery of this Circular shall not, under any circumstances, create any implication that there has been no change in the affairs of Drax Group plc since the date of this Circular or that the information in it is correct as of any subsequent time.

J.P. Morgan Securities plc (which conducts its UK investment banking activities as J.P. Morgan Cazenove), which is authorised and regulated in the United Kingdom by the Financial Conduct Authority, is acting exclusively for Drax and for no one else in connection with the Acquisition and will not regard any other person (whether or not a recipient of this Circular) as a client in relation to the Acquisition and will not be responsible to anyone other than Drax for providing the protections afforded to customers of J.P. Morgan Cazenove or for affording advice in relation to the Acquisition, the contents of this Circular or any transaction, arrangement or other matter referred to in this Circular.

Save for the responsibilities and liabilities, if any, of J.P. Morgan Cazenove under FSMA or the regulatory regime established under FSMA, J.P. Morgan Cazenove assumes no responsibility whatsoever and makes no representations or warranties, express or implied, in relation to the contents of this Circular, including its accuracy, completeness or verification or for any other statement made or purported to be made by Drax, or on Drax's behalf, or by J.P. Morgan Cazenove, or on J.P. Morgan Cazenove's behalf, and nothing contained in this Circular is, or shall be, relied on as a promise or representation in this respect, whether as to the past or the future, in connection with Drax or the Acquisition. J.P. Morgan Cazenove disclaims to the fullest extent permitted by law all and any responsibility and liability whether arising in tort, contract or otherwise which it might otherwise be found to have in respect of this Circular.

This Circular contains forward-looking statements relating to the Drax Group, the ScottishPower Generation Group, the Enlarged Group and the Acquisition. Statements containing the words "intends", "believes", "anticipates", "may", "will", "estimates", "expects" and "outlook" and words of similar meaning are forward-looking. By their nature, all forward-looking statements are subject to assumptions, risks and uncertainties. Although Drax believes that the expectations reflected in these forward-looking statements are reasonable, there can be no assurance that these expectations will prove to have been correct and because these statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by those forward-looking statements. The preceding sentence does not qualify the statement in section 9 of Part VIII (*Additional Information*) of this Circular. Each forward-looking statement speaks only as of the date of the particular statement. Drax does not undertake any obligation publicly to update or revise any forward-looking statement as a result of new information, future events or other information, although such forward-looking statements will be publicly updated if required by the Financial Conduct Authority, the Listing Rules and the Disclosure and Transparency Rules, the rules of the London Stock Exchange or by applicable law.

Percentages in tables have been rounded and accordingly may not add up to 100 per cent. Certain financial data have also been rounded. As a result of this rounding, the totals of data presented in this Circular may vary slightly from the actual arithmetic totals of such data.

Capitalised terms have the meaning ascribed to them in Part IX (*Definitions*) of this Circular.

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## EXPECTED TIMETABLE OF PRINCIPAL EVENTS

Date of this Circular	5 December 2018
Latest time and date for receipt of Forms of Direction	10.00am on 17 December 2018
Latest time and date for receipt of Forms of Proxy or Crest Proxy Instructions	10.00am on 19 December 2018
General Meeting	10.00am on 21 December 2018
Expected date of Completion	31 December 2018

### NOTES:

Unless otherwise stated, references to times in this Circular are to London time.

Future dates are indicative only and are subject to change by Drax, in which event details of the new times and dates will be notified to the FCA and, where appropriate, Shareholders.

## DIRECTORS, COMPANY SECRETARY, REGISTERED OFFICE AND ADVISERS

<b>Directors</b>	Philip Cox CBE Will Gardiner Andy Koss David Lindsell Tim Cobbold Tony Thorne Nicola Hodson David Nussbaum Vanessa Simms	<i>Chairman</i> <i>Group Chief Executive Officer</i> <i>Chief Executive Officer, Drax Power</i> <i>Senior Independent Non-Executive Director</i> <i>Independent Non-Executive Director</i> <i>Independent Non-Executive Director</i> <i>Independent Non-Executive Director</i> <i>Independent Non-Executive Director</i>
<b>General Counsel and Group Company Secretary</b>	David McCallum	
<b>Registered office</b>	Drax Power Station Selby North Yorkshire YO8 8PH	
<b>Sponsor and financial adviser</b>	J.P. Morgan Cazenove 25 Bank Street Canary Wharf London E14 5JP	
<b>Legal adviser</b>	Slaughter and May One Bunhill Row London EC1Y 8YY	
<b>Reporting accountants</b>	Deloitte LLP 1 New Street Square London EC4A 3HQ	
<b>Registrars</b>	Equiniti Limited Proxy Department Aspect House Spencer Road Lancing West Sussex BN99 6DA	

**PART I**  
**LETTER FROM THE CHAIRMAN OF DRAX GROUP PLC**  
**DRAX GROUP PLC**

*(Incorporated and registered in England and Wales with registered number 5562053)*

*Registered office:*

**Drax Group plc**  
Drax Power Station  
Selby  
North Yorkshire YO8 8PH

*Directors:*

Philip Cox CBE	<i>Chairman</i>
Will Gardiner	<i>Group Chief Executive Officer</i>
Andy Koss	<i>Chief Executive Officer, Drax Power</i>
David Lindsay	<i>Senior Independent Non-Executive Director</i>
Tim Cobbold	<i>Independent Non-Executive Director</i>
Tony Thorne	<i>Independent Non-Executive Director</i>
Nicola Hodson	<i>Independent Non-Executive Director</i>
David Nussbaum	<i>Independent Non-Executive Director</i>
Vanessa Simms	<i>Independent Non-Executive Director</i>

5 December 2018

Dear Shareholder,

**Proposed Acquisition of ScottishPower Generation Limited**

**1. Introduction**

On 16 October 2018, Drax announced that it had agreed to acquire ScottishPower's portfolio of pumped storage, hydro and gas-fired generation assets for £702 million in cash from Iberdrola S.A. Drax will be acquiring the ScottishPower Generation Group, which comprises SPGEN and its wholly owned subsidiary, SMW. On 3 December 2018, Drax announced that it had reached agreement with Iberdrola S.A. on revised terms for the Acquisition, to reflect the suspension of payments under the Capacity Market with effect from 15 November 2018 following the ruling of the General Court of the European Union.

The Acquisition constitutes a Class 1 transaction under the Listing Rules. As a consequence, Completion of the Acquisition is conditional on the Acquisition receiving the approval of Shareholders. Accordingly, you will find set out at the end of this Circular a notice convening a General Meeting to be held at the offices of FTI Consulting, 200 Aldersgate Street, London EC1A 4HD at 10.00am on 21 December 2018.

Completion of the Acquisition is expected (subject to the approval by Shareholders) to take place on 31 December 2018.

I am writing to you on behalf of the Board to give you details of the Acquisition, including the background to and reasons for the Acquisition, and to explain why the Board considers the Acquisition to be in the best interests of Drax and its Shareholders as a whole.

You should read the whole of this Circular and not rely solely on the summarised information contained in this Part I (*Letter from the Chairman of Drax Group plc*).

**2. Background to and reasons for the Acquisition**

**Background**

The assets included in the Portfolio are Cruachan pumped storage hydro (440MW), run-of-river hydro locations at Galloway and Lanark (126MW), four CCGT stations, Damhead Creek (805MW), Rye House (715MW), Shoreham (420MW) and Blackburn Mill (60MW), and a biomass-from-waste facility (Daldowie).

As the UK energy system transitions towards renewable technologies, the demand for flexible, secure energy sources is set to grow. The Board believes there is a compelling logic in adding further flexible sources of power to Drax's offering, which will accelerate our ability to deliver our strategic vision of a lower-carbon, lower-cost energy future for the UK. The Acquisition will allow Drax to make the most of growing opportunities in system support for the UK energy system, and to diversify its generation capacity in order to become a multi-site, multi-technology operator. The Board believes that the Acquisition makes great financial and strategic sense, and expects to deliver material value to our shareholders through long-term earnings and attractive returns.

### **Key benefits of the Acquisition**

#### *A leading provider of flexible, low-carbon and renewable generation in the UK*

The UK has a target to reduce carbon emissions by 80 per cent. by 2050. The transition to a low-carbon economy requires decarbonisation of heating, transport and generation. This will in turn require additional low-carbon sources of generation to be developed in the UK. The Intergovernmental Panel on Climate Change projects that by 2050 as much as 85 per cent. of future global electricity generation could come from renewable sources – predominantly wind and solar. This transition will lead, at times, to high levels of power price volatility and increasing demand for system support services. Managing an energy system with these characteristics will only be possible if it is supported by the right mix of flexible assets to manage volatility, balance the system and provide the crucial non-generation services which a stable energy system requires.

The Acquisition is closely aligned with this structural need and the operation of Drax's existing biomass generation and gas options. The combination of the Portfolio and our existing assets will allow the Drax Group to provide more of the flexibility increasingly required by the UK energy system to enable higher levels of intermittent renewable generation while also offering the Drax Group increased exposure to the growing need for system support and power price volatility.

#### *Increased earnings potential aligned with the Drax Group's strategy and UK energy needs*

The Acquisition is in line with the Drax Group's strategy to create value from flexible, low-carbon and renewable generation. The Acquisition will provide Drax with an increased level of low-carbon and renewable capacity, and contract-based system support revenues, providing improved earnings visibility. This positions Drax to capture value by supporting the system operator in managing the impact of the UK's transition to a low-carbon economy, as the share of wind and solar generation increases.

#### *High-quality earnings and returns*

For the year ended 31 December 2017, the Portfolio generated EBITDA of £36 million. EBITDA in 2019 is expected to be higher due to incremental contracted capacity payments (c.£42 million), no availability restrictions (Cruachan's access to the UK grid during 2017 was limited by network transformer works) (c.£8 million), a lower level of corporate cost charged to the Portfolio (c.£9 million) and revenues from system support services and current power prices. Pumped storage and hydro activities represent a significant proportion of the earnings associated with the Portfolio, with the pumped storage and hydro assets, in the opinion of the Directors, representing most of the value of the Acquisition. When combined with renewable earnings and system support income from existing biomass generation, the Acquisition is expected to lead to an overall increase in the quality of earnings from the Enlarged Group (although in the short-term earnings will be affected by uncertainty related to the Capacity Market). Further information on the preparation of the 2017 EBITDA can be found in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*).

Based on the Board's expectations of the position that is most likely to be achieved in relation to the Capacity Market following the Capacity Market Ruling (the most likely outcome being that the European Commission will re-approve the existing Capacity Market in its current form or a broadly similar form. Further information in this regard can be found in section 3 of this Part I (*Letter from the Chairman of Drax Group plc*)), the Board believes the Acquisition represents an attractive opportunity to create significant value for Shareholders and is expected to deliver returns significantly in excess of the Drax Group's weighted average cost of capital. The Acquisition strengthens the Drax Group's ability to pay a growing and sustainable dividend. Drax remains committed to its capital allocation policy and to its current £50 million share buy-back programme, with around £43 million of shares (including dealing and associated costs) purchased as at the Latest Practicable Date.

The Board has considered other possible outcomes for the Capacity Market which are less likely but may ensue and if they do the financial effects of the Acquisition may be adversely affected. The Board believes that if the more plausible of these other outcomes were to ensue the returns from the Acquisition would still be in excess of the Drax Group's weighted average cost of capital. The Board has not attempted to quantify the effects if the less plausible of these other outcomes were to ensue, if there were no Capacity Market or similar mechanism, or if significant structural changes were made to the Capacity Market, all of which it views as a remote possibility. The Board notes that in those circumstances it believes the loss or reduction of Capacity Market payments could be mitigated by increases in wholesale power prices.

Based on recent power and commodity prices and assuming that all contracted capacity payments are received (although this is subject to material uncertainty as described below), the Portfolio is expected to generate EBITDA in 2019 in a range of £90 million to £110 million,<sup>1</sup> from gross profits of £155 million to £175 million, of which around two thirds is expected to come from non-commodity market sources, including system support services, capacity payments, ROCs and Daldowie. Due to the contract-based nature of many of these services, Drax expects to improve earnings visibility through non-commodity earnings streams, while retaining significant opportunity to benefit from power price volatility. If, in light of the Capacity Market Ruling, the contracted capacity payments payable in 2019 in respect of the Portfolio are not received or accrued in 2019, the expected EBITDA for the Portfolio in 2019 would be reduced by up to £47 million (from a range of £90 million to £110 million) down to a range of £43 million to £63 million before considering mitigating factors. Further information on the preparation of the profit forecasts above can be found in Part VII (*Profit Forecasts*).

#### *Diversified generation and portfolio benefits*

The Acquisition accelerates Drax's development from a single-site generation business into a multi-site, multi-technology operator. With the acquisition of the Portfolio, a fall in gas prices could be mitigated by an increase in gas-fired generation reflecting the relative dispatch economics of the different technologies.

Drax also expects to benefit from the management of generation across a broader asset base, leveraging the Drax Group's expertise in the operation, trading and optimisation of large dispatchable generation. Drax believes that the team operating the Portfolio has a strong engineering culture which is closely aligned with the Drax model and will enhance the Drax Group's strong capabilities across engineering disciplines. About 260 operational roles will transfer to Drax as part of the Acquisition, complementing and reinforcing Drax's existing engineering and operational capabilities.

### **3. Impact of the Capacity Market Ruling on the Acquisition**

On 15 November 2018, the General Court of the European Union issued a ruling annulling the European Commission's 2014 decision not to undertake a more detailed investigation of the UK Government's scheme establishing the Capacity Market (the "**Capacity Market Ruling**"). The Capacity Market Ruling imposed a "standstill period" while the European Commission completes a further State aid investigation into the Capacity Market. Payments to generators scheduled under existing capacity agreements and the holding of future capacity auctions have been suspended.

Contracted capacity payments make up a significant proportion of the earnings of the ScottishPower Generation Group, with many of the assets in the Portfolio benefitting from the right to receive such payments under existing capacity agreements. For the period from 1 January 2019 to 30 September 2022, the Cruachan pumped storage hydro asset has contracted capacity payments of £29 million, the Galloway run-of-river hydro assets have contracted capacity payments of £5 million, and the Damhead Creek, Rye House, Shoreham and Blackburn CCGT assets have contracted capacity payments of £122 million in aggregate.

The Board notes the UK Government's statement in response to the Capacity Market Ruling that it is working closely with the European Commission to aid their investigation and to seek a timely State aid re-approval decision for the Capacity Market. The UK Government also confirmed that the Capacity Market Ruling does not change its belief that Capacity Market auctions are the most

<sup>1</sup> 2019 EBITDA is stated before any allocation of Group overheads (as these will be an allocation of the existing Drax Group cost base which is not expected to increase as a result of the acquisition of the Portfolio).



appropriate way to deliver secure electricity supplies at the lowest cost. The UK Government also noted that the Capacity Market Ruling was decided on procedural grounds and did not constitute a direct challenge to the design of the Capacity Market mechanism itself.<sup>2</sup>

National Grid has confirmed that the T-4 and T-1 auctions for the years 2022/23 and 2019/20, which were scheduled for February 2019 and January 2019 respectively, have been postponed in light of the “standstill period”. National Grid has advised capacity agreement holders that the UK Government is doing everything in its power to re-obtain State aid approval as soon as possible, and that the UK Government intends to seek a separate State aid approval to run a one-off “replacement” T-1 Auction in 2019. The Board notes that National Grid has also confirmed that it intends to run the postponed T-4 for 2022/23 as a T-3 Auction in the 2019 auction round, subject to the European Commission completing its formal investigation and providing State aid approval for the Capacity Market.<sup>3</sup>

The UK Government confirmed it is working to reinstate the full Capacity Market regime and is in discussions with the European Commission regarding the swiftest means of doing so.

Based on the information available to it and legal advice it has received, the Board believes the most likely outcome is that the European Commission will re-approve the existing Capacity Market in its current form or a broadly similar form. The Board recognises there is some uncertainty whether, if the Capacity Market is reinstated in its current form, the contracted capacity payments for the Capacity Market year 2018/2019 which are currently suspended will be paid by the UK Government. To mitigate the risk that these payments are not received for the 2018/2019 Capacity Market year, Drax has agreed with Iberdrola S.A. certain amendments to the Acquisition Agreement signed on 16 October 2018. A summary of the principal terms of the Acquisition (as amended) is set out below in section 4 of this Part I (*Letter from the Chairman of Drax Group plc*). The Board believes that the arrangements provided in the amended Acquisition Agreement mitigate in economic terms the majority of the risk that those suspended capacity payments will not be paid.

The Board believes that the most likely outcome after 2019 is that existing capacity agreements for the period to 2022 will be honoured but recognises that a range of other outcomes is possible, from re-running the auctions for delivery years 2019/2020, 2020/2021 and 2021/2022 to a significant revision of the structure of the Capacity Market. In each case, the exact impact of these changes cannot be predicted. However, the Board notes the UK Government’s commitment to ensuring there is a capacity market in some form.

#### **4. Summary of the principal terms of the Acquisition**

##### *Acquisition Agreement*

The Acquisition Agreement was entered into on 16 October 2018 between Drax Smart Generation and the Seller and was amended on 3 December 2018. Pursuant to the Acquisition Agreement, the Seller has agreed to sell, and Drax Smart Generation has agreed to acquire, the whole of the issued share capital of SPGEN for £702 million, subject to certain customary adjustments in respect of cash, debt and working capital.

The Acquisition is conditional on: (a) the approval of the Acquisition by Shareholders, which is required as the Acquisition constitutes a Class 1 transaction under the Listing Rules; and (b) the CMA having indicated in response to pre-Completion engagement by Drax that it has no further questions at that stage or the CMA having provided a decision that the Acquisition will not be subject to a reference under the UK merger control regime. On 1 November 2018, the CMA indicated to Drax that it had no further questions at that stage, which resulted in this condition being satisfied. Completion is therefore currently expected to occur on 31 December 2018 assuming that the shareholder approval condition is satisfied by that date.

Drax Smart Generation has the right to terminate the Acquisition Agreement upon the occurrence of a material reduction in available generation capacity at any of the Cruachan, Galloway and Lanark or Damhead Creek facilities which subsists, or is reasonably likely to subsist, for a

<sup>2</sup> The UK Government’s press release can be found at <https://www.gov.uk/government/collections/electricity-market-reform-capacity-market>.

<sup>3</sup> The published advice of National Grid in relation to the Capacity Market Ruling can be found at <https://www.emrdeliverybody.com/cm/home.aspx> and <https://www.emrdeliverybody.com/Prequalification/Advice%20for%20capacity%20agreement%20holders%20and%20capacity%20market%20applicants%20v1.1.pdf>.

continuous period of three months. The right of Drax Smart Generation to terminate in these circumstances is subject to the Seller's right to defer Completion if the relevant material reduction in available generation capacity can be resolved by end of the month following the anticipated date of Completion.

A break fee of £14.6 million (equal to 1 per cent. of Drax's market capitalisation at close of business on 15 October 2018, being the day before announcement of the Acquisition) is payable if the Shareholders fail to approve the Acquisition, save where this is as a result of a material reduction in available generation capacity as described above.

The Seller has given certain customary covenants in relation to the period between signing of the Acquisition Agreement and Completion, including to carry on the SPGEN business in the ordinary and usual course. The Seller will also carry out certain reorganisation steps prior to Completion. The Seller has provided customary warranties, as well as indemnities in respect of certain specific matters, including for any losses associated with the reorganisation referred to above. A customary tax covenant is also provided in the Acquisition Agreement.

Drax Group Holdings has agreed to guarantee the payment obligations of Drax Smart Generation under the Acquisition Agreement. Scottish Power UK plc has agreed to guarantee the payment obligations of the Seller under the Acquisition Agreement.

#### *Arrangements in respect of Capacity Market Payments*

Drax Smart Generation and the Seller have agreed that Capacity Market payments due to the ScottishPower Generation Group in respect of the period from 1 October 2018 to Completion that are received by the Drax Group after Completion will be passed through to the Seller.

Drax Smart Generation and the Seller have also agreed to share the risk in relation to Capacity Market payments due to the ScottishPower Generation Group in respect of the period from Completion to 30 September 2019. If less than 100 per cent. of these Capacity Market payments is received and the gross profit of the ScottishPower Generation Group in 2019 (the "**2019 Gross Profit**") is lower than expected, Drax Smart Generation will receive a payment from the Seller up to £26 million. The mechanism also gives the Seller the opportunity to earn an upside of up to the same amount if less than 100 per cent. of these Capacity Market payments is received but the ScottishPower Generation Group performs better than expected in 2019.

Under these arrangements, if less than 100 per cent. of these Capacity Market payments is received:

- (A) the Seller will make a payment to Drax Smart Generation if the 2019 Gross Profit is less than £155 million. The payment will be an amount equal to 72.2 per cent. of any shortfall in the 2019 Gross Profit below £155 million. The amount of the payment is capped at the lower of the amount in respect of Capacity Market payments due to the ScottishPower Generation Group but not received and £26 million; and
- (B) Drax Smart Generation will make a payment to the Seller if the 2019 Gross Profit is more than £165 million. The payment will be an amount equal to 72.2 per cent. of any amount by which the 2019 Gross Profit exceeds £165 million. The amount of the payment is capped at the lower of the amount in respect of Capacity Market payments due to the ScottishPower Generation Group but not received by the Drax Group and £26 million.

A provisional payment will be made in December 2019, with a true-up payment to be made when the audited accounts of the ScottishPower Generation Group for the year ending 31 December 2019 have been finalised. If, subsequent to such settlement, the Drax Group receives any Capacity Market Payments in respect of the period 1 January 2019 to 30 September 2019, Drax will pay 72.2 per cent. of those amounts to the Seller capped at the amount paid by the Seller to Drax Smart Generation under the mechanism above.

Any payments pursuant to the mechanism above will be cash adjustments to the consideration and not included in EBITDA.

Further details of the Acquisition Agreement are set out in section 1 of Part IV (*Principal Terms of the Acquisition*).

#### **Transitional Services Agreement**

The Seller and SPGEN will enter into a transitional services agreement effective at Completion. Further details of the Transitional Services Agreement are set out in section 2 of Part IV (*Principal Terms of the Acquisition*).

## 5. Financing of the Acquisition

Drax Corporate has entered into the Acquisition Facility Agreement, a fully underwritten £725 million secured acquisition debt facility to finance the Acquisition, with a term of twelve months from the first date of utilisation of the facility (with a seven-month extension option) and interest payable at a rate of LIBOR plus the applicable margin. The margin will step up after three, six, twelve and seventeen months following the first date of utilisation of the facility, and ranges from 0.75 per cent. per annum to 2.75 per cent. per annum. The facility is competitively priced and below Drax's current cost of debt.

Drax will consider potential options for its long-term financing strategy in 2019. Assuming performance in line with current expectations and if all Capacity Market Payments due in 2019 are received before the end of 2019, net debt to EBITDA is expected to fall to Drax's long-term target of around 2x by the end of 2019. If Capacity Market payments are not received in 2019, net debt to EBITDA is expected to fall to around 2x during 2020. Following announcement of the Acquisition on 16<sup>th</sup> October 2018, S&P and Fitch affirmed Drax Group Holding's corporate rating of BB+.

Drax has hedged 1TWh of the commodity exposures in the Portfolio ahead of Completion.

Further details of the Acquisition Facility Agreement are set out in paragraph 7.1(B) of Part VIII (*Additional Information*).

## 6. Current trading and outlook

### 6.1 Drax

Following the Capacity Market Ruling, £7 million of contracted capacity payments relating to 2018, principally in relation to Drax's remaining two coal-fired units, will not be paid as and when expected. Taking this into account and following Drax's recent good trading performance and assuming continued good operational availability for the remainder of the year, Drax's full year EBITDA outlook remains in line with previous expectations, with net debt to EBITDA now expected to be around 1.5x for the full year, excluding the impact of the Acquisition.

Further information on Drax's 2018 Profit Forecast (including the basis of preparation and the underlying assumptions) is set out in Part VII (*Profit Forecasts*).

### 6.2 ScottishPower Generation Group

Throughout 2018, availability for the Portfolio has been ahead of ScottishPower Generation Group management expectations, allowing the assets to benefit from rising short-term power prices and balancing market activities when providing system support services. Spark spreads margins from gas generation were lower reflecting rising gas and carbon prices resulting in lower year-on-year output.

The Portfolio's contracted capacity payments for the 1 October 2018 to 31 December 2018 period, which have been suspended following the Capacity Market Ruling, are expected to be around £12.7 million gross.

The Portfolio is expected, based on recent power and commodity prices and assuming that all contracted capacity payments are received (although this is subject to material uncertainty as described below), to generate, for the year ending 31 December 2019, EBITDA in a range of £90-110 million, and gross profits of £155 million to £175 million, of which around two thirds is expected to come from non-commodity market sources, including system support services, capacity payments, Daldowie and ROCs. Pumped storage and hydro activities represent a significant proportion of the earnings associated with the portfolio. If, in light of the Capacity Market Ruling, the contracted capacity payments payable in 2019 in respect of the Portfolio are not received or accrued in 2019, the expected EBITDA for the Portfolio in 2019 would be reduced by up to £47 million (from a range of £90 million to £110) million down to a range of £43 million to £63 million before considering mitigating factors.

Further information on the 2019 Profit Forecast (including the basis of preparation and the underlying assumptions and further details on the sensitivity of this profit forecast to the impact of the Capacity Market Ruling) is set out in Part VII (*Profit Forecasts*).

## **7. Costs and risks relating to the Acquisition**

Whilst the Board considers the Acquisition to be in the best interests of Drax and its Shareholders as a whole, there are a number of potential risks and uncertainties that Shareholders should consider before voting on the Resolution. Your attention is drawn to the further discussion of certain of these risks and uncertainties set out in Part II (*Risk Factors*).

In particular, the Capacity Market Ruling has created uncertainty in relation to a significant proportion of the Portfolio's anticipated earnings. While the beliefs set out in section 3 of this Part I (*Letter from the Chairman of Drax Group plc*) reflect the Board's best estimate of the likely outcome of the European Commission's re-investigation of the Capacity Market, the results of this re-investigation, which will turn on a detailed analysis of the Capacity Market as well as the specific information received during the European Commission's consultation of interested parties, are uncertain.

Following Completion, the ScottishPower Generation Group will be integrated into the Drax Group and, although Drax is developing a detailed integration plan, as with any integration exercise this process may present both expected and unexpected challenges and costs. In addition, it is possible that, even after integration of the businesses, the expected benefits of the Acquisition might take longer than anticipated to realise or might not be realised.

As set out above, the Enlarged Group will have further indebtedness due to the new financing under the Acquisition Facility Agreement and will be required to service interest payments in respect of this. Following announcement of the Acquisition on 16 October 2018, S&P and Fitch affirmed Drax Group Holding's corporate rating of BB+.

Drax will also incur a number of other customary costs in relation to the Acquisition more generally (including legal, accounting, financial adviser, sponsor and other transaction fees), some of which will be payable regardless of whether the Acquisition reaches Completion.

## **8. General Meeting**

Set out at the end of this Circular is a Notice convening the General Meeting which is to be held at the offices of FTI Consulting, 200 Aldersgate Street, London EC1A 4HD on 21 December 2018 at 10.00am, at which the Resolution will be proposed. The Resolution is set out in full at the end of this Circular in the Notice of General Meeting. As a Class 1 transaction for the purposes of the Listing Rules, the Acquisition may only be completed if it is first approved by Shareholders. Voting on the Resolution will be taken on a poll, rather than a show of hands, to reflect the number of shares held by a Shareholder, whether or not the Shareholder is able to attend the meeting. The Resolution requires the approval of a majority of the votes cast (in person or by proxy) at the meeting in order to be passed.

## **9. Action to be taken**

Whether or not you propose to attend the General Meeting, you are requested to:

- (A) complete, sign and return the enclosed Form of Proxy in accordance with the instructions printed thereon and contained in this Circular so as to be received by the Registrars no later than 10.00am on 19 December 2018;
- (B) register the appointment of your proxy electronically via the internet at [www.sharevote.co.uk](http://www.sharevote.co.uk), where full instructions are given. Please note that the personalised numbers printed at the top of the Form of Proxy will be required and instructions must be received by no later than 10.00am on 19 December 2018; or
- (C) if you hold shares in CREST you may appoint a proxy by completing and transmitting a CREST Proxy Instruction to the Registrars (CREST participant ID RA19) so that it is received by no later than 10.00am on 19 December 2018.

The return of a completed Form of Proxy, electronic proxy appointment or CREST Proxy Instruction will not prevent you from attending the General Meeting and voting in person if you wish to do so. Share Incentive Plan participants are unable to attend the meeting unless they hold shares registered in their own name.

## 10. Financial advice

The Board has received financial advice from J.P. Morgan Cazenove in relation to the Acquisition. In providing their financial advice to the Board, J.P. Morgan Cazenove has relied upon the Board's commercial assessment of the Acquisition.

## 11. Recommendation

In the Board's opinion, the Acquisition is in the best interests of Shareholders as a whole. Accordingly, the Board unanimously recommends Shareholders to vote in favour of the Resolution to be proposed at the General Meeting, as the Directors intend to do in respect of their own beneficial shareholdings of Ordinary Shares, being in aggregate 230,024 Ordinary Shares, representing approximately 0.056491% of Drax's issued ordinary share capital as at the Latest Practicable Date.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Philip Cox', written in a cursive style.

Philip Cox CBE  
Chairman

## PART II RISK FACTORS

*Prior to making any decision to vote in favour of the Resolution at the General Meeting, Shareholders should carefully consider, together with all other information contained in this Circular, the specific factors and risks described below.*

*Drax considers these to be the material risk factors relating to the Acquisition for Shareholders to consider. These should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. There may be other risks of which the Board is not aware or which it believes to be immaterial which may, in the future, be connected to the Acquisition and have a material and adverse effect on the business, financial condition, results of operations or future prospects of the Enlarged Group after the Acquisition. The risks described below relate only to the Acquisition and are not set out in any particular order.*

*If any or a combination of these risks actually materialise, the business, operations, financial condition and prospects of the Drax Group or the ScottishPower Generation Group could be materially and adversely affected to the detriment of the Drax Group and the Shareholders. Additional risks and uncertainties which are not known to the Directors as at the date of this Circular, or that the Directors currently deem immaterial, may also have a material adverse effect on the Drax Group or the ScottishPower Generation Group if they materialise. If this occurs, the market price of Ordinary Shares could decline and you may lose all or part of your investment.*

*The information given is as of the date of this Circular and, except as required by the FCA, the London Stock Exchange, the Listing Rules, the DTRs or any other law or regulation, will not be updated.*

### 1. RISKS RELATED TO THE ACQUISITION

#### ***The Acquisition is conditional and may not proceed***

Completion remains conditional upon the passing of the Resolution at the General Meeting. In the event that this condition is not satisfied by the Long Stop Date (or such later time as the parties to the Acquisition Agreement may agree), the Acquisition Agreement will automatically terminate.

In addition, Drax Smart Generation has retained the right to terminate the Acquisition Agreement in the event of a material reduction in available generation capacity at the Cruachan, Galloway and Lanark or Damhead Creek facilities which subsists, or is reasonably likely to subsist, for a continuous period of three months. The right of Drax Smart Generation to terminate in these circumstances is subject to the Seller's right to defer Completion if the relevant material reduction in available generation capacity can be resolved by the end of the month following the anticipated date of Completion.

#### ***A break fee may be payable if the Acquisition does not complete***

In the event that the Acquisition does not complete due to the non-satisfaction of the shareholder approval condition, a break fee of £14.6 million (equal to 1 per cent. of Drax's market capitalisation at close of business on 15 October 2018, being the day before announcement of the Acquisition) will be payable by Drax Smart Generation to the Seller, subject to limited exceptions.

#### ***The Drax Group may incur losses and other costs in unwinding certain hedging arrangements if the Acquisition does not complete***

In anticipation of Completion occurring, the Drax Group has hedged 1TWh of commodity exposures which are associated with the Portfolio. In the event that the Acquisition does not complete, these hedging arrangements would no longer be required by the Drax Group and the Drax Group may incur losses and other costs in unwinding such hedging arrangements.

#### ***The Enlarged Group may not realise, or it may take the Enlarged Group longer to realise, the expected benefits of the Acquisition***

The Enlarged Group may fail to achieve certain or any of the anticipated benefits that Drax expects to realise as a result of the Acquisition, including as a result of poor performance by the

ScottishPower Generation Group, or it may take longer than expected to realise those benefits. If the anticipated benefits, such as the anticipated financial returns, are not achieved, or take longer than expected to be realised, this could have a material adverse impact on the Enlarged Group's business, financial condition, results of operations and prospects.

***The Enlarged Group may experience operational difficulties in integrating the ScottishPower Generation Group into the Drax Group***

The Drax Group and the ScottishPower Generation Group currently operate and, until Completion, will continue to operate as separate and independent businesses. The Acquisition will lead to the incorporation of the ScottishPower Generation Group into the Drax Group and the evolution of the Drax Group's generation business from a single site generation model to a multi-site model. The success of the Enlarged Group will depend, in part, on the success of that integration and the ability of the Enlarged Group to realise the anticipated benefits from combining the two businesses.

Whilst initial work on integration has begun, more detailed analysis will need to be undertaken before a detailed integration plan is finalised and can be implemented. The integration process is likely to present administrative, managerial and financial challenges, some of which may not be identified until after the process is under way. Unforeseen difficulties, costs, liabilities, losses or delays could adversely affect the business of the Enlarged Group and the realisation of the benefits of the Acquisition.

Potential difficulties in the integration process include:

- consolidating and integrating procedures, systems, accounting functions, compensation structures for transferring staff and other policies;
- putting in place the necessary new systems and/or processes to enable the Enlarged Group to dispatch electricity from (and where applicable, offtake gas from the gas transmission network to supply) generating assets located across Great Britain from a central hub;
- replacing IT infrastructure (notably network connections and certain pieces of hardware at the acquired generation sites that will be removed or retained by the Seller following the expiry of any transitional arrangements under the TSA);
- operating and integrating different technology platforms and systems across an Enlarged Group with a significantly increased geographical footprint; and
- disruption to the ongoing business of the Drax Group and the ScottishPower Generation Group.

The failure of, or any delays or difficulties encountered in connection with, the integration process could also lead to reputational damage to the Enlarged Group.

***The Enlarged Group will have increased debt financing***

Following Completion, the Enlarged Group will have further indebtedness due to the inclusion in the Enlarged Group of the new financing under the Acquisition Facility Agreement taken out by Drax Corporate to finance the Acquisition. The Enlarged Group will accordingly be required to service interest payments in respect of the Acquisition Facility.

The increased financial indebtedness of the Enlarged Group may result in operational constraints for the Enlarged Group going forward, which may adversely affect the business, financial condition, results of operations and prospects of the Enlarged Group.

The Acquisition Facility Agreement has a term of twelve months from the first date of utilisation of the Acquisition Facility (with a seven-month extension option) and there can be no guarantee that the Enlarged Group will be able to refinance the Acquisition Facility Agreement on optimal terms or at an optimal time due to wider economic and market factors outside the Enlarged Group's control.

***Drax's acquisition and integration costs may be greater than anticipated***

Drax expects to incur a number of costs in relation to the Acquisition, including the cost of integrating the ScottishPower Generation Group into the Drax Group in order to combine the

operations of Drax and the ScottishPower Generation Group successfully. The actual costs of the integration process may exceed those estimated and there may be further additional and/or unforeseen expenses incurred in connection with the Acquisition.

In addition, Drax will incur legal, accounting, technical engineering adviser, financial adviser, sponsor and other transaction fees and costs relating to the Acquisition. Some of these costs will be payable regardless of whether the Acquisition reaches Completion.

While Drax believes that the integration and acquisition costs will be more than offset by the realisation of the benefits resulting from the Acquisition, this net benefit may not be realised in the short term or at all (particularly if the Acquisition does not proceed) or may be less than anticipated. This could affect the business, financial condition, results of operations and prospects of Drax and, following Completion, the Enlarged Group.

***Management attention may be diverted from the business of the Drax Group by the Acquisition***

The Acquisition has required, and will continue to require, substantial amounts of both time and focus from the Drax Group management team, which could adversely affect their ability to operate each respective business effectively and efficiently. The Enlarged Group's management will also be required to devote significant attention and resources to integrating the two businesses. There is a risk that the challenges associated with managing the Acquisition will result in management distraction and that consequently the underlying businesses will not perform in line with expectations.

***Adverse change in the condition of the ScottishPower Generation Group***

Drax Smart Generation may only terminate the Acquisition Agreement prior to Completion in the event of a material reduction in available generation capacity at the Cruachan, Galloway and Lanark or Damhead Creek facilities or if the conditions to Completion under the Acquisition Agreement are not satisfied. Completion is expected to occur on 31 December 2018, subject to the passing of the Resolution at a General Meeting of the Shareholders.

While Drax Smart Generation has certain consent rights over the actions taken by the ScottishPower Generation Group prior to Completion, Drax will not own or run the ScottishPower Generation Group until Completion. It is possible that there could be an adverse event affecting the ScottishPower Generation Group which would not give rise to a right of Drax Smart Generation to terminate the Acquisition. In such circumstances, the value of the ScottishPower Generation Group may be less than anticipated.

**2. RISKS RELATING TO THE DRAX GROUP, THE SCOTTISHPOWER GENERATION GROUP AND/OR THE ENLARGED GROUP FOLLOWING THE ACQUISITION**

This section documents those risks and uncertainties currently faced by the Drax Group and, following the Acquisition, the Enlarged Group, which are potentially impacted by the Acquisition.

***The current status of the Capacity Market in the UK is uncertain***

On 15 November 2018, the General Court of the European Union issued a ruling annulling the European Commission's 2014 decision not to undertake a more detailed investigation of the UK Government's scheme establishing the Capacity Market. The Capacity Market Ruling imposed a "standstill period" while the European Commission completes a further State aid investigation into the Capacity Market. Payments to generators scheduled under existing capacity agreements and the holding of future capacity auctions have been suspended.

Contracted capacity payments make up a significant proportion of the earnings of the ScottishPower Generation Group, with many of the assets in the Portfolio benefitting from the right to receive such payments under existing capacity agreements. For the period from 1 January 2019 to 30 September 2022, the Cruachan pumped storage hydro asset has contracted capacity payments of £29 million, the Galloway run-of-river hydro assets have contracted capacity payments of £5 million, and the Damhead Creek, Rye House, Shoreham and Blackburn CCGT assets have contracted capacity payments of £122 million in aggregate.



Drax's investment case for the Acquisition takes account of these capacity payments. Based on the information available to it and legal advice it has received, the Board believes the most likely outcome is that the European Commission will re-approve the existing Capacity Market in its current form or a broadly similar form. The Board recognises there is some uncertainty whether, if the Capacity Market is reinstated in its current form, the contracted capacity payments for the Capacity Market year 2018/2019 which are currently suspended will be paid by the UK Government. However, the Board believes that the most likely outcome after 2019 is that existing capacity agreements for the period to 2022 will be honoured. While this reflects the Board's best estimate of the likely outcome of the European Commission's re-investigation, the results of this investigation, which will turn on a detailed analysis of the Capacity Market as well as the specific information received during the European Commission's consultation of interested parties, are uncertain.

It is not possible to predict with certainty the duration of the European Commission's re-investigation. The duration of the current suspension of payments and auctions is therefore uncertain. Capacity payments expected to be received by the Enlarged Group in 2019 could be delayed for an extended period, and the Capacity Market arrangements agreed in the Acquisition Agreement would not be sufficient to compensate for the lost contracted payments, impacting the financial results of the Enlarged Group.

Even if the European Commission grants a new State aid clearance in relation to the Capacity Market, there is no guarantee that the capacity payments suspended between the date of the Capacity Market Ruling and the date of the new clearance will be paid to generators. This will depend both on the outcome of the European Commission's investigation and on the UK Government's response thereto. In the event that suspended capacity payments are not paid, the Capacity Market arrangements agreed in the Acquisition Agreement would not be sufficient to compensate for the lost contracted payments.

Any new clearance of the Capacity Market granted by the European Commission may be subject to conditions that the form of the Capacity Market is amended from its current design. This may include the condition that existing capacity agreements are invalidated and that current and future capacity auctions need to be re-run. In these circumstances, there would be no guarantee that any amended form of Capacity Market would provide comparable contracted payments to those the Enlarged Group expects to receive under the existing Capacity Market, that future capacity auctions would be re-run on terms comparable to the existing Capacity Market or that the Enlarged Group would be successful in those re-run auctions. In these circumstances, the Capacity Market arrangements agreed in the Acquisition Agreement would not be sufficient to compensate for the lost contracted payments.

If the Capacity Market is not reinstated, it may be replaced by a new mechanism which is not as advantageous to the Enlarged Group. If no new clearance is given by the European Commission, and/or no new capacity market mechanism is introduced, the Enlarged Group will be more exposed to wholesale electricity prices due to the reduction in contracted revenue streams. In these circumstances, the Capacity Market arrangements agreed in the Acquisition Agreement would not be sufficient to compensate for the lost contracted payments.

Each of these outcomes has the potential to have a material adverse impact on the Enlarged Group's business, financial condition, results of operations and prospects.

#### ***The cost of debt financing could increase or financing could cease to be available***

The ability of the Drax Group (and, following Completion, the Enlarged Group) to operate its business depends in part on being able to raise funds. While the Drax Group currently seeks to maintain a balance between continuity of funding and flexibility through the use of borrowings with a range of maturities, there can be no assurance, particularly in the current economic environment, that, over the longer term, the Enlarged Group will be able to find lenders who are willing to lend on no worse terms than its existing financing arrangements, or at all, or that existing financing arrangements (including the Acquisition Facility Agreement) will be able to be refinanced on no worse terms, or at all, upon or prior to maturity.

An increase in the cost, or lack of availability, of finance and capital could have a material adverse effect on the Enlarged Group's business, financial condition and results of operations in the medium to long term.

***The Enlarged Group may become exposed to increased regulatory risk***

The Enlarged Group will operate in a highly regulated market subject to detailed legislation and regulation. Following Completion, the size of the Enlarged Group's business will increase. The increased size of the Enlarged Group, and particularly its increased presence in wholesale generation and the ancillary services markets, may lead to increased risk of regulatory scrutiny or risk arising from regulatory change, as regulators seek to ensure sufficient market liquidity in order to ensure effective price competition. In particular, some industry regulation and generator licence conditions only apply to larger generation groups. Increased regulatory scrutiny may lead to an increased cost of compliance and may result in actions against the Enlarged Group for non-compliance with the regulatory framework. The Enlarged Group may also become increasingly exposed to the impact of changes to the legal or regulatory framework in which the Enlarged Group will operate. This could have a material adverse impact on the Enlarged Group's business, financial condition, results of operations and prospects.

In addition, the Acquisition will increase the breadth of regulatory oversight of the Enlarged Group compared with that faced by the Drax Group currently. In particular, the Enlarged Group will be subject to regulations on a range of assets (for example, dams, reservoirs and watercourses) that are not currently within the purview of the Drax Group. Whilst operational staff are transferring as part of the Acquisition, any failure of the Enlarged Group to adapt to the increased regulatory burden may result in non-compliance and have a material adverse effect on the Enlarged Group's business, financial condition and results of operations.

***The earnings of the ScottishPower Generation Group may be impacted by disruptive technologies in an evolving wholesale electricity market***

A proportion of the ScottishPower Generation Group's earnings are derived from the Cruachan facility's provision of ancillary services and its wider participation in the balancing market. Such revenues derive from the fact that pumped storage is the only storage technology that forms a notable proportion of the current UK wholesale generation mix and is the only storage technology in the UK that is able to discharge at full load for significant lengths of time.

There are a number of nascent electricity storage technologies in development across the world (for example, lithium-ion battery technology) that may, in the future, have the necessary scale and reliability to compete with pumped storage facilities. Whilst Drax's investment case for the Acquisition takes account of emerging technologies, should these technologies displace pumped storage earlier or at a greater rate than anticipated, this could have a material adverse effect on the Enlarged Group's business, financial condition and results of operations.

***The geographical location and configuration of certain of the generating assets may lead to longer unplanned outages than a typical similar outage at the Drax Group's existing generation site***

Certain of the assets of the ScottishPower Generation Group, particularly the Cruachan facility, are located in remote areas and are of a complex configuration. Technical failures of key components at such facilities (for example, failures of high-voltage transformers) may lead to longer and more significant disruptions in generation than Drax is accustomed to due to the increased delay associated with acquiring, transporting and installing replacement components in such locations and facilities. The unexpected occurrence of a significant component failure may therefore have a material adverse effect on the Enlarged Group's business, operations, prospects, financial condition and results of operations.

***A more diverse generation and operating portfolio increases the scope of the health and safety and environmental obligations applicable to the Enlarged Group, and a failure of the Enlarged Group to adapt to those obligations may materially impact the financial condition of the Enlarged Group***

Whilst Drax has historically maintained high standards of health and safety and environmental compliance in respect of its existing generation and operational assets, the Enlarged Group will be subject to an increased regulatory burden in this area as a result of acquiring a more diversified generation and operational portfolio across both England and Scotland. A failure by the Enlarged

Group to adapt to, and comply with, this increased regulatory burden or else adequately to remedy any legacy issues with the acquired sites may result in fines or criminal sanctions which, if levied, would have a material adverse effect on the Enlarged Group's business, operations, prospects, financial condition and results of operations.

***It may be difficult for the Enlarged Group to retain or attract appropriately qualified personnel to fulfil the requirements of the Enlarged Group***

Certain of the generation assets of the Enlarged Group are in remote locations and require employees with sufficient technical engineering and operational expertise to maintain and operate them safely and optimally. Whilst operational staff are transferring as part of the Acquisition, there can be no certainty that such staff will continue to work for the Enlarged Group in the longer term, and it may prove difficult to find adequately skilled replacements.

Separately, the new multi-site, multi-fuel generation model to be operated by the Enlarged Group will require an adequate number of sufficiently qualified employees to dispatch the larger and more complex portfolio of assets optimally. Energy trading on this scale is a highly specialised field and it may be difficult for the Enlarged Group to retain or attract the personnel required.

***The performance of the ScottishPower Generation Group's pumped storage and hydro assets could be impacted by unseasonal or extreme weather conditions***

The economic case underpinning the acquisition of the pumped storage and hydro generation assets assumes that the assets will be generally capable of being dispatched at times of peak demand and pricing. However, unseasonal or extreme weather may prevent this. If, for example, droughts restrict water flows and consequent generation or excess rainfall leads to a need to dispatch the assets at sub-optimal times to avoid flooding, this could have a material adverse effect on the Enlarged Group's business, operations, prospects, financial condition and results of operations.

***The result of the UK referendum on withdrawal from the EU may have a negative effect on economic conditions, financial markets and demand for the Enlarged Group's products and services, which could materially adversely affect the business, results of operations and financial condition of the Enlarged Group***

Following Completion, the Enlarged Group will be based in and operate principally within the UK. The Enlarged Group will be particularly exposed to UK-wide risks.

Brexit and prolonged periods of uncertainty relating to the UK's withdrawal from the EU could result in significant macroeconomic deterioration. This could adversely affect demand for electricity and will directly impact the financial condition of the Enlarged Group's customers, which could have a negative impact on its revenues. A significant weakening of economic conditions in the UK accompanied by higher insolvency rates could also result in a decrease in energy consumption, which could adversely affect the Enlarged Group's performance.

The UK's post-Brexit relationship with the EU has yet to be finally defined and there are a number of risks which the Enlarged Group's business may face as a result. If the UK were to leave the EU customs union, this could result in new or increased tariffs being levied on the Enlarged Group's imports of wood pellets. Furthermore, the Enlarged Group has finite storage capacity at ports and at Drax Power Station and delays in unloading vessels at ports caused by the imposition of other non-tariff barriers (such as higher documentation requirements or more time-consuming custom checks) risk causing disruption to the Enlarged Group's wider biomass supply chain and the ability of the Enlarged Group to ensure that Drax Power Station has sufficient fuel to generate at its optimal levels.

Brexit may also impact liquidity in the UK electricity and gas markets, as a result of "market decoupling" between the UK and the rest of the EU and reduce liquidity in derivative markets to the extent that the terms of Brexit prevent the Enlarged Group's counterparties from trading in the UK under the EU's passporting rules for financial services firms.

The effects of Brexit could be significant as the UK Government would no longer be subject to the set of EU directives, which commit the EU member states to reducing carbon emissions, increasing energy efficiency and increasing renewable energy production. Any change in the UK Government's policy towards renewable energy targets could have a material adverse effect on the Enlarged Group's business, operations, prospects, financial condition and results of operations.

## PART III INFORMATION ON THE SCOTTISHPOWER GENERATION GROUP

### 1. Overview

The ScottishPower Generation Group, which includes SPGEN and SMW, SPGEN's wholly owned subsidiary, comprises a portfolio of flexible, low-carbon and renewable generation assets located in the UK with a capacity of up to 2.6GW across pumped storage, hydro and gas-fired generation. The portfolio comprises:

- **Cruachan pumped storage hydro-electric power station:** commissioned in 1965 and located in Argyll and Bute, Scotland, Cruachan is capable of generating 440MW of large-scale storage and flexible electricity. The power station is built into the hollowed-out rock of the mountain, Ben Cruachan. It uses electricity from the grid at times of low demand to pump water from Loch Awe, to its storage reservoir part way up the mountain. Water is also collected from the surrounding hills. At times of peak demand, water is released from the reservoir through the station's turbines to generate electricity.

Cruachan provides contracted ancillary services to the UK energy market including fast reserve and frequency response. The station also provides system support services through the balancing market in addition to merchant power generation. Cruachan has £29 million of contracted capacity payments for the period from 1 January 2019 to 30 September 2022. Cruachan, which provides over 35 per cent. of the UK's pumped storage by volume, can provide long-duration storage with the ability to achieve full load in 30 seconds, which it can maintain for over 16 hours, making it a strategically important asset remunerated by a broad range of non-commodity based revenues.

Cruachan's total capacity of 440MW is split between four units, two of which generate up to 120MW, and the other two up to 100MW. Cruachan has four primary modes of operation, which can deliver a range of balancing and ancillary services. The plant can switch between the modes to meet commercial requirements or as required by NGET. This flexibility is highly valued. Prices for the various services provided by Cruachan were increased early in 2018 and the plant has seen no diminution in demand, underlining its strategic value. Cruachan, as well as the Galloway and Lanark assets described below, are expected to operate for a very long time, as hydro and pumped storage assets generally operate for prolonged periods provided adequate levels of investment are maintained.

- **Galloway and Lanark run-of-river hydro-electric power stations:** commissioned in 1935 and 1926 respectively, and located in south-west Scotland, Galloway and Lanark are distribution-connected stations capable of generating up to a combined 126MW of stable renewable electricity. Lanark (17MW) benefits from index-linked ROC revenues extending until 2027. Galloway (109MW), in addition to renewable power generation, operates a reservoir and dam system providing power storage capabilities and opportunities for peaking and system support services. It has £5 million of contracted capacity payments for the period from 1 January 2019 to 30 September 2022.
- **CCGT power stations:** Damhead Creek (805MW), Rye House (715MW) and Shoreham (420MW), all located in south-east England, are together capable of generating up to 1,940MW of electricity. These assets provide baseload and peak power generation in addition to other system support services and benefit from grid access income associated with their location in south-east England where energy demand is highest. The three plants have contracted capacity payments of £118 million for the period from 1 January 2019 to 30 September 2022. These CCGT power stations are supported by long-term maintenance contracts with the original equipment manufacturers. The operating teams have an excellent track record of managing those contracts to extract maximum value for the running regimes, which have changed over time.

Damhead Creek has held frequency response contracts with NGET and is regularly used in the balancing mechanism for energy and system services. The site also benefits from an option for the development of a second CCGT asset, Damhead Creek II, which would provide additional gas generation optionality for Drax, alongside Drax's existing coal-to-gas repowering and OCGT projects. Damhead Creek II has prequalified for the 2019 Capacity Market auction along with two of Drax's existing OCGT projects.

- **Other smaller sites:** these include a small CCGT in Blackburn (60MW), which has contracted capacity payments of £4 million for the period from 1 January 2019 to 30 September 2022, and a 50,000 tonne biomass-from-waste facility in Daldowie, which converts waste water into processed sludge pellets and benefits from a firm offtake agreement until 2026.

## 2. Regulation

SPGEN holds an electricity generation licence granted under section 6(1)(a) of the Electricity Act 1989 to generate electricity for the purpose of giving a supply to any premises or enabling a supply to be given. The Cruachan, Galloway and Lanark assets are also operated under licences issued by the Scottish Environment Protection Agency to implement the requirements of the Water Framework Directive (2000/60/EC).

## 3. Employees and pensions

Within the ScottishPower Generation Group, there are currently 194 employees employed by SPGEN (not counting those who work at the site located in Hatfield and will transfer out of the ScottishPower Generation Group back to the Seller's group when that site is transferred back to the Seller's group as part of the pre-sale reorganisation) and 65 employees employed by SMW at the Daldowie site. Further information on the pre-sale reorganisation is set out at paragraphs 1.7 and 1.9 of Part IV (*Principal Terms of the Acquisition*).

The most senior employees within the ScottishPower Generation Group are the heads of UK Hydro and of UK Thermal, who are the regional managers overseeing the different hydro and thermal sites. Other senior employees include the O&M managers (who are specific site managers) and technical specialist managers, comprising among others the engineering managers, plant managers, asset optimisation & innovation managers and performance & compliance managers.

The Seller's group operates one defined contribution retirement benefit scheme, and two defined benefit schemes, the SPPS and the Manweb Scheme. Both of the ScottishPower Generation Group companies are currently participating in these arrangements, with contributions for the defined benefit schemes based on pension costs across all of the participating companies. The ScottishPower Generation Group will cease participating in the Manweb Scheme following the transfer out of the ScottishPower Generation Group of certain assets and associated employees located at Hatfield which do not form part of the Acquisition.

Drax Smart Generation has agreed to assume the accrued defined benefit pension liabilities associated with the employees of the ScottishPower Generation Group in the SPPS. Following Completion, the ScottishPower Generation Group will continue to participate in the SPPS for an interim period while new pension arrangements are set up by Drax for the benefit of the relevant ScottishPower Generation Group employees. More details on these arrangements can be found in paragraph 1.10 of Part IV (*Principal Terms of the Acquisition*).

## PART IV PRINCIPAL TERMS OF THE ACQUISITION

The following is a summary of the principal terms of the Acquisition Agreement.

### 1. Acquisition Agreement

#### 1.1 Parties and structure

The Acquisition Agreement was entered into on 16 October 2018 between Drax Smart Generation and the Seller. Pursuant to the Acquisition Agreement, the Seller has agreed to sell, and Drax Smart Generation has agreed to acquire, the whole of the issued share capital of SPGEN. The Acquisition Agreement was amended on 3 December 2018 pursuant to the Acquisition Agreement Amendment Deed.

Drax Group Holdings has agreed to guarantee the payment obligations of Drax Smart Generation under the Acquisition Agreement. Scottish Power UK plc has agreed to guarantee the payment obligations of the Seller under the Acquisition Agreement.

#### 1.2 Consideration

At Completion, Drax Smart Generation will pay the Seller the sum of £702 million in cash (the debt-free/cash-free price), as adjusted to account for estimated net cash, estimated net debt and the amount by which estimated working capital differs from a target level of working capital. This initial amount of consideration will be subject to customary adjustments post-Completion to reflect the actual amounts of net cash, net debt and working capital of the ScottishPower Generation Group at Completion, such adjustments to be determined in a completion statement to be prepared after Completion.

#### 1.3 Capacity Market payments

In response to the Capacity Market Ruling, the following arrangement (the “**Capacity Market Arrangement**”) has been included in the Acquisition Agreement as part of the amendments agreed on 3 December 2018.

##### Capacity Market payments relating to the period before Completion

If, following Completion, the Drax Group receives any Capacity Market payments to which the ScottishPower Generation Group is entitled in respect of the period from 1 October 2018 to 31 December 2018 (or, if Completion occurs in 2019, the date of Completion) (the “**Pre-Completion Capacity Market Payments**”), the Drax Group will procure that an amount equal to such Pre-Completion Capacity Market Payments is paid to the Seller within twenty business days of receipt by the Drax Group of those Pre-Completion Capacity Market Payments.

##### Capacity Market payments relating to the period from Completion until 30 September 2019

If less than 100 per cent. of the Capacity Market payments due to the ScottishPower Generation Group in respect of the period from 1 January 2019 to 30 September 2019 (the “**2019 Capacity Market Payments**”) are received by the Drax Group by 15 December 2019, the Capacity Market Arrangement provides for the following payment to be made by the Seller or by Drax Smart Generation (as applicable).

The Seller will pay to the Drax Group the lower of: (i) the amount of 2019 Capacity Market Payments not received; and (ii) one of the following:

- (A) if the ScottishPower Generation Group gross profit for the financial year ending 31 December 2019 (the “**2019 Gross Profit**”) is equal to or less than £119 million, an amount equal to £26 million;
- (B) if the 2019 Gross Profit is more than £119 million but less than £155 million, an amount equal to £26 million less an amount which is 72.22 per cent. of the amount by which the 2019 Gross Profit exceeds £119 million; or
- (C) if the 2019 Gross Profit is equal to or more than £155 million, zero.

Drax Smart Generation will pay to the Seller the lower of: (i) the amount of 2019 Capacity Market Payments not received; and (ii) one of the following:

- (D) if the 2019 Gross Profit is less than £165 million, zero;
- (E) if the 2019 Gross Profit is equal to or more than £165 million but less than £201 million, an amount equal to 72.22 per cent. of the difference between the 2019 Gross Profit and £165 million; or
- (F) if the 2019 Gross Profit is equal to or more than £201 million, an amount equal to £26 million.

#### ***Procedure for payments between Seller and Drax***

A provisional payment under the Capacity Market Arrangement will be made by the relevant party by no later than 15 December 2019 on the basis of estimates of gross profit prepared by the Drax Group and notified to the Seller. A final calculation will be made in March 2020 on the basis of the audited accounts of the ScottishPower Generation Group for the year ending 31 December 2019 and an adjusting payment made, if required.

If, after the final settlement under the Capacity Market Arrangement has been made, the Drax Group receives any 2019 Capacity Market Payments, the Drax Group will procure that an amount equal to 72.22 per cent. of such 2019 Capacity Market Payments is paid to the Seller up to the amount that the Seller has paid to the Drax Group pursuant to the Capacity Market Arrangement.

#### ***General***

Following Completion, the Seller will have sole conduct of any claims in relation to Capacity Market payments that the ScottishPower Generation Group may have against the UK Government, the European Commission or any other third party in respect of the Pre-Completion Capacity Market Payments and, if and for so long as the Seller is liable to make or has made a payment to the Drax Group under the Capacity Market Arrangement, in respect of the 2019 Capacity Market Payments.

The Drax Group has agreed that until the final settlement under the Capacity Market Arrangement, it will manage the ScottishPower Generation Group in good faith and in the ordinary course of business and in a manner which does not frustrate, manipulate or distort the operation of the operation of the Capacity Market Arrangement or the profitability of the ScottishPower Generation Group.

### **1.4 Conditions to Completion**

The Acquisition is conditional on:

- (A) the passing of the Resolution approving the Acquisition by Shareholders; and
- (B) the CMA having indicated in response to pre-Completion engagement by Drax that it has no further questions at that stage or the CMA having provided a decision that the Acquisition will not be subject to a reference under the UK merger control regime.

On 1 November 2018, the CMA indicated to Drax that it had no further questions at that stage, which resulted in the relevant condition being satisfied. In the event that the shareholder approval condition is not or cannot be satisfied by the Long Stop Date (or such later date as the parties may agree), the Acquisition Agreement will automatically terminate.

Completion is currently expected to occur on 31 December 2018.

### **1.5 Termination for material reduction in available generation capacity**

Drax Smart Generation has the right to terminate the Acquisition Agreement upon the occurrence of a material reduction in available generation capacity at any of the Cruachan, Galloway and Lanark or Damhead Creek facilities which subsists, or is reasonably likely to subsist, for a continuous period of three months. The right of Drax Smart Generation to terminate in these circumstances is subject to the Seller's right to defer Completion if the relevant material reduction in available generation capacity can be resolved by end of the month following the anticipated date of Completion (or, if earlier, the Long Stop Date). If the material reduction in available generation capacity is still continuing on that deferred date of Completion, Drax Smart Generation may exercise its termination right under the Acquisition Agreement.



## **1.6 Break fee**

A break fee of £14.6 million (equal to 1 per cent. of Drax's market capitalisation at close of business on 15 October 2018, being the day before announcement of the Acquisition) is payable if the shareholder approval condition is not met, save where this is as a result of a material reduction in available generation capacity as described above.

## **1.7 Pre-sale reorganisation**

The Seller has agreed to complete a pre-sale reorganisation (under which certain assets have been transferred, or are in the process of being transferred, into and out of the ScottishPower Generation Group, including the transfer out of sites located in Hatfield and Avonmouth) as soon as reasonably practicable.

## **1.8 Seller's warranties and tax covenant**

### Warranties; liability caps and time limits for warranty claims

The Seller has provided customary warranties, subject to certain limitations. Fundamental warranties (being those warranties relating to the Seller's legal title to, and capacity to sell, the SPGEN shares) are capped at the total amount of consideration payable under the Acquisition Agreement. For all other warranties, a cap of 20 per cent. of the total amount of consideration applies, with a further 10 per cent. available in respect of property title warranties. The fundamental warranties, property title warranties and tax warranties have a seven year time limit, while all other warranties have an eighteen-month time limit. The Seller has also undertaken to pay specific remediation costs in respect of the Daldowie site.

### Tax covenant

The Acquisition Agreement includes a customary tax covenant from the Seller to provide protection for Drax Smart Generation against the pre-Completion tax liabilities of the ScottishPower Generation Group. The tax covenant is subject to customary general limitations, including a cap on all tax covenant claims set at the total amount of consideration payable under the Acquisition Agreement together with a seven-year time limit for bringing any tax covenant claim.

## **1.9 Seller's indemnities**

### Pre-sale reorganisation indemnity

The Seller has provided an indemnity to cover all losses incurred by the ScottishPower Generation Group or Drax as a result of the pre-sale reorganisation not being completed fully and in accordance with all legal requirements. This indemnity is uncapped and is for a duration of 10 years in respect of environmental liabilities and seven years for all other liabilities.

### Pension indemnity

The Seller has also provided an indemnity in relation to the ScottishPower Generation Group's potential pension obligations. Further information is provided in paragraph 1.10 below.

## **1.10 Pensions and pensions indemnity**

### Assumption of pension liabilities

Drax Smart Generation has agreed to assume the accrued defined benefit pension liabilities associated with the employees of the ScottishPower Generation Group as at the date of signing the Acquisition Agreement. Following Completion, the ScottishPower Generation Group will continue to participate in the Seller's group defined benefit pension scheme, known as the SPPS, for an interim period of twelve months unless agreed otherwise while a new defined benefit pension scheme, the New Scheme, is set up by the ScottishPower Generation Group for the benefit of its employees. At the end of the interim period, the SPPS trustees will be requested to transfer from the SPPS to the New Scheme an amount of liabilities (and corresponding share of

assets) agreed between the Seller and Drax Smart Generation (or failing agreement, an amount determined by an independent actuary) in respect of the past service liabilities relating to the ScottishPower Generation Group employees.

If the amount of assets the SPPS trustees transfer to the New Scheme is less than the amount agreed (or independently determined), the Seller has agreed to pay Drax Smart Generation the difference (plus Bank of England base rate interest). If the amount of assets the SPPS trustees transfer to the New Scheme is more than the amount agreed (or independently determined), Drax Smart Generation has agreed to pay the Seller the difference (plus Bank of England base rate interest).

If the SPPS trustees do not make any transfer to the New Scheme within the period of eighteen months following the interim period (unless this was caused by a breach of the Acquisition Agreement by the Seller), Drax Smart Generation has agreed to pay £16 million (plus Bank of England base rate interest) to the Seller as compensation for the SPPS liabilities not taken on by the New Scheme.

In accordance with its legislative obligations, the ScottishPower Generation Group has agreed to provide its employees who have “protected person” status with future defined benefit pension accrual under the New Scheme.

#### Pension indemnity

The Seller has agreed to indemnify Drax Smart Generation in respect of certain liabilities of the ScottishPower Generation Group and of the Drax Group which may arise in respect of the SPPS and the Manweb Scheme (in which the ScottishPower Generation Group has participated before Completion). This indemnity will remain in place for eight years after Completion and is capped at the total amount of consideration payable under the Acquisition Agreement.

### **1.11 Seller’s pre-Completion obligations**

Prior to Completion, the Seller is required to ensure that the ScottishPower Generation Group carries out its business in the ordinary course, in accordance with past practice and Prudent Operating Practice. The Acquisition Agreement also includes wide restrictions on pre-Completion dealings by the ScottishPower Generation Group (including material deviations from an agreed capital expenditure plan, amendments to or entry into material contracts, dealings with employees, incurrence of indebtedness and certain tax matters), in each case without Drax Smart Generation’s consent.

## **2. Transitional Services Agreement**

At Completion, the Seller will enter into the TSA with SPGEN. Under the TSA, the Seller will use its best efforts to provide the Drax Group and the ScottishPower Generation Group with services that should, in principle, be the same services provided to the ScottishPower Generation Group in the twelve months before Completion. Under the TSA, the Seller will also provide assistance in relation to the extraction and separation of the ScottishPower Generation Group from the systems of the Seller and integration of the ScottishPower Generation Group onto the systems of the Drax Group. Services provided under the TSA are expected to be charged on the basis of actual cost, provided that certain extensions to the agreed term of any service will result in the charges for such an extended service being increased by 5 per cent. per month up to a maximum increase of 20 per cent. above the initial cost price.

**PART V**  
**HISTORICAL FINANCIAL INFORMATION RELATING TO THE SCOTTISHPOWER**  
**GENERATION GROUP**

**Part A: Historical Financial Information relating to the ScottishPower Generation Group**

The ScottishPower Generation Group comprises ScottishPower Generation Limited (“**SPGEN**”) and its wholly owned subsidiary, SMW Limited (“**SMW**”). For the purposes of this Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) only, the ScottishPower Generation Group is referred to as the “**Target Group**”.

The financial information contained in this Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) does not constitute statutory accounts within the meaning of section 434(3) of the Companies Act 2006. The statutory accounts of both SPGEN and SMW, each in respect of the years ended 31 December 2017, 2016 and 2015, have been delivered to the Registrar of Companies.

Shareholders should read the whole of this Circular and not rely solely on the financial information contained in this Part V (*Historical Financial Information relating to the ScottishPower Generation Group*).

**COMBINED INCOME STATEMENT OF THE TARGET GROUP**

	Notes	Years ended 31 December		
		2017 £m	2016 £m	2015 £m
Revenue	<b>1</b>	641.3	622.4	707.7
Fuel costs in respect of generation		(294.8)	(313.2)	(294.6)
Grid charges		(36.7)	(39.7)	(35.5)
Other energy supply costs		(201.8)	(164.1)	(259.8)
Total cost of sales		(533.3)	(517.0)	(589.9)
<b>Gross Profit</b>		<b>108.0</b>	<b>105.4</b>	<b>117.8</b>
Operating and administrative expenses	<b>3</b>	(52.7)	(51.6)	(51.5)
Overheads allocated by Related Parties <sup>1</sup>	<b>3</b>	(19.2)	(19.5)	(17.5)
<b>EBITDA<sup>2</sup></b>		<b>36.1</b>	<b>34.3</b>	<b>48.8</b>
Depreciation	<b>6</b>	(16.7)	(14.3)	(16.5)
Amortisation	<b>7</b>	(0.7)	(0.5)	(0.6)
Asset obsolescence charges		(0.8)	(0.9)	(0.8)
Gains on disposal		1.6	—	0.3
Unrealised losses on derivative contracts	<b>17</b>	—	—	(14.2)
<b>Operating Profit</b>		<b>19.5</b>	<b>18.6</b>	<b>17.0</b>
Interest payable and similar charges	<b>4</b>	(6.8)	(6.3)	(11.7)
Interest receivable	<b>4</b>	0.1	—	—
Foreign exchange gains/losses	<b>4</b>	—	(0.2)	(0.1)
<b>Profit before tax</b>		<b>12.8</b>	<b>12.1</b>	<b>5.2</b>
Total tax credit/(charge)	<b>5</b>	1.0	(0.8)	4.3
<b>Profit for the year attributable to equity holders</b>		<b>13.8</b>	<b>11.3</b>	<b>9.5</b>

All results relate to continuing operations.

1 “Related Parties” refers to entities that are members of the group of companies headed by Iberdrola S.A. See note 21 for further details.

2 EBITDA is defined as profit before interest, tax, depreciation, amortisation, unrealised gains and losses on derivative contracts and material or one-off items that do not reflect the underlying trading performance of the business.

## COMBINED STATEMENT OF COMPREHENSIVE INCOME OF THE TARGET GROUP

	Notes	Years ended 31 December		
		2017 £m	2016 £m	2015 £m
<b>Profit for period</b>		<b>13.8</b>	<b>11.3</b>	<b>9.5</b>
<b>Items that will not be subsequently reclassified to profit or loss:</b>				
Actuarial losses on defined benefit pension scheme	15	(2.2)	(1.9)	0.1
Deferred tax on actuarial losses on defined benefit pension scheme	5	0.4	0.4	—
<b>Items that may be subsequently reclassified to profit or loss:</b>				
Fair value gains/(losses) on cash flow hedges		0.1	2.9	(0.8)
Deferred tax on cash flow hedges	5	—	(0.6)	0.2
<b>Other comprehensive (expense)/income for the period</b>		<b>(1.7)</b>	<b>0.8</b>	<b>(0.5)</b>
<b>Total comprehensive income for the period attributable to equity holders</b>		<b>12.1</b>	<b>12.1</b>	<b>9.0</b>

## COMBINED BALANCE SHEET OF THE TARGET GROUP

	Notes	As at 31 December		
		2017 £m	2016 £m	2015 £m
<b>Assets</b>				
<b>Non-current assets</b>				
Intangible assets	7	1.0	1.2	0.9
Property, plant and equipment	6	274.2	270.4	266.7
Other investments		—	0.2	0.2
Derivative financial instruments	17	0.3	0.1	—
		<b>275.5</b>	<b>271.9</b>	<b>267.8</b>
<b>Current assets</b>				
Trade and other receivables	8	20.7	18.0	18.0
Amounts receivable from Related Parties	8	117.0	98.5	104.9
Inventories	11	1.0	0.9	0.7
Derivative financial instruments	17	—	—	0.9
Current tax assets		1.3	2.0	4.4
		<b>140.0</b>	<b>119.4</b>	<b>128.9</b>
<b>Total Assets</b>		<b>415.5</b>	<b>391.3</b>	<b>396.7</b>
<b>Liabilities</b>				
<b>Current liabilities</b>				
Trade and other payables	9	29.2	33.6	28.4
Amounts payable to Related Parties	9	113.6	66.4	113.2
Borrowings from Related Parties	10	402.4	520.3	437.0
Provisions	14	0.4	0.1	—
Derivative financial instruments	17	—	—	0.5
		<b>545.6</b>	<b>620.4</b>	<b>579.1</b>
<b>Net current liabilities</b>		<b>(405.6)</b>	<b>(501.0)</b>	<b>(450.2)</b>
<b>Non-current liabilities</b>				
Trade and other payables	9	0.3	0.4	0.5
Borrowings from Related Parties	10	100.0	—	—
Provisions	14	12.0	11.7	10.6
Deferred tax liabilities	5	4.8	5.0	1.9
Retirement benefit obligations	15	6.6	5.9	4.6
		<b>123.7</b>	<b>23.0</b>	<b>17.6</b>
<b>Net liabilities</b>		<b>(253.8)</b>	<b>(252.1)</b>	<b>(200.0)</b>
<b>Total invested capital and reserves deficit attributable to equity holders of the Target Group</b>		<b>(253.8)</b>	<b>(252.1)</b>	<b>(200.0)</b>

## COMBINED STATEMENT OF CHANGES IN EQUITY OF THE TARGET GROUP

	Invested Capital/(Deficit) £m
<b>At 1 January 2015</b>	<b>(686.0)</b>
Total comprehensive income for the year	9.0
Capital contribution	500.0
Capital distribution	(23.0)
<b>At 1 January 2016</b>	<b>(200.0)</b>
Total comprehensive income for the year	12.1
Capital distribution	(64.2)
<b>At 1 January 2017</b>	<b>(252.1)</b>
Total comprehensive income for the year	12.1
Capital distribution	(13.8)
<b>At 31 December 2017</b>	<b>(253.8)</b>

## COMBINED CASH FLOW STATEMENT OF THE TARGET GROUP

	Notes	Years ended 31 December		
		2017 £m	2016 £m	2015 £m
<b>Cash generated from/(absorbed by) operations</b>	<b>12</b>	<b>54.2</b>	<b>9.0</b>	<b>(50.7)</b>
Income taxes refunded		3.6	6.6	7.0
Interest paid		(5.5)	(11.8)	(12.3)
Interest received		0.1	—	—
<b>Net cash from operating activities</b>		<b>52.4</b>	<b>3.8</b>	<b>(56.0)</b>
<b>Cash flows from investing activities</b>				
Purchases of property, plant and equipment		(20.5)	(19.7)	(21.1)
Purchases of intangible assets		(0.3)	(0.9)	(0.2)
Proceeds from sale of property, plant and equipment		1.7	—	—
<b>Net cash used in investing activities</b>		<b>(19.1)</b>	<b>(20.6)</b>	<b>(21.3)</b>
<b>Cash flows from financing activities</b>				
(Decrease)/increase in amounts due to related parties		(19.5)	81.0	(399.7)
Proceeds from invested capital		—	—	500.0
Distributions from invested capital		(13.8)	(64.2)	(23.0)
<b>Net cash (absorbed by)/generated from financing activities</b>		<b>(33.3)</b>	<b>16.8</b>	<b>77.3</b>
<b>Net change in cash and cash equivalents</b>		<b>—</b>	<b>—</b>	<b>—</b>
Cash and cash equivalents at 1 January and 31 December		—	—	—

## Introduction

### Basis of preparation

Whilst the entities and assets within the Target Group are under common control they have not previously constituted a single group which has prepared consolidated financial results. The following key corporate transactions have been considered when preparing the historical financial information.

- In March 2016, as part of a group restructuring exercise to transfer all of ScottishPower Energy Wholesale's generating activities to one legal entity, the Shoreham Power Station assets and liabilities of ScottishPower (SCPL) Limited (a subsidiary of SPGEN at the time) and the Damhead Creek Power Station assets of ScottishPower (DCL) Limited (another Iberdrola group company) were purchased by SPGEN. The financial results, position and cash flows of these assets, which form part of the acquisition, have been included in each period presented in the historical financial information, as if they had always formed part of the Target Group.
- In July 2018, certain assets (principally legacy coal-fired power stations) and associated trading were disposed of from the Target Group. The financial results, position and cash flows of the businesses that are not to be acquired have been excluded from the historical financial information in its entirety.
- In addition, the historical financial information excludes the financial results, position and cash flows of certain other assets (principally the Hatfield gas storage business and industrial land located in Avonmouth) that are not to be acquired and are in the process of being disposed of from the Target Group pursuant to the pre-sale reorganisation process described in paragraphs 1.7 and 1.9 of Part IV (*Principal Terms of the Acquisition*).

Accordingly, the historical financial information of the Target Group, which has been prepared specifically for the purposes of this Circular, does not constitute statutory accounts within the meaning of section 434(3) of the Companies Act 2006.

The combined historical financial information for the three years ended 31 December 2017 has been prepared in accordance with the Listing Rules and Prospectus Directive Regulation together with International Financial Reporting Standards ("**IFRS**"). The application of these conventions results in the following departure from IFRS (in all other respects, IFRS has been applied):

- As a result of the treatment of the key corporate transactions, described above, the combined historical financial information does not strictly comply with the requirements of IFRS 10 'Consolidated Financial Statements'. However, the combined historical financial information has been prepared on a basis that applies the consolidation principles of IFRS 10.
- IFRS does not explicitly provide guidance for the preparation of combined historical financial information. Certain accounting conventions, permitted for the preparation of historical financial information for inclusion in investment circulars as described in the Standards for Investment Reporting Annexure (the "**Annexure**"), have been applied where IFRS does not provide specific accounting treatments.

The combined historical financial information for the Target Group has been prepared for three years ended 31 December 2017 on an aggregated basis, in accordance with the Annexure. The aggregation process was as follows:

- the assets and liabilities, income and expenses, and cash flows of SPGEN and SMW were consolidated in accordance with IFRS 10 Consolidated Financial Statements;
- the assets and liabilities together with the associated reserves, income and expenses, and cash flows of the Shoreham Power Station and Damhead Creek Power Station which were acquired in March 2016 were included within the historical financial information for the three-year period ended 31 December 2017 in accordance with the carve-out considerations of paragraph 26 of the Annexure;
- the assets and liabilities together with the associated reserves, income and expenses, and cash flows of certain assets, which were subsequently disposed of by the Target Group in July 2018 (and will not be acquired by Drax Group as part of the Acquisition), were removed from the historical financial information in accordance with the carve out considerations of paragraph 27 of the Annexure;



- the majority of the Target Group's revenue was derived from, and commodity purchasing requirements procured from, another ScottishPower company which traded with third parties. A significant amount of central overheads was also levied on an aggregate basis to the Target Group. Where transactions were not clearly identifiable as relating to the specific power stations and other assets not acquired, a method to most fairly allocate these costs to the carved out operations (on the basis of the share of pre-carve-out revenue or employees as most applicable) was applied in accordance with paragraph 33 of the Annexure;
- an actuarial calculation of the pension costs arising from the employees involved in the purchased assets was determined and accounted for in accordance with paragraph 41 of the Annexure with a detailed actuarial calculation prepared in respect of the 2017 historical financial information and consistently applied in respect of the prior years;
- reflecting the carving out of certain operations subsequently disposed of by the Target Group the Invested Capital/(Deficit) represents a combination of the balances associated with the equity holders of the Target Group, rather than an analysis of reserves; and
- intercompany transactions and balances within the Target Group have been eliminated.

The principal accounting policies applied in the preparation of the historic financial information are set out below. These policies are (excluding the adjustments identified above) the accounting policies adopted by Drax in its last audited annual financial statements, being for the year ended 31 December 2017, and have been consistently applied to all the periods presented unless otherwise stated.

The financial statements are presented in sterling (£) and rounded to the nearest £0.1 million, or where required, the nearest £'000.

### **Going concern**

The Directors have considered the Enlarged Group's working capital forecasts and projections, taking account of reasonably possible changes in trading performance. They are satisfied that the Enlarged Group (which includes the Target Group) has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they have adopted the going concern basis in preparing the combined historical financial information.

### **Accounting policies**

The historical financial information has been prepared on the historical cost basis, except for derivative financial instruments measured at fair value. Those accounting policies that are material to the historical financial information are set out in the relevant note. A full listing of new standards, interpretations and pronouncements under IFRS applicable to the historical information is presented in note 20.

### **Judgements, estimates and uncertainties**

The preparation of the historical information requires management to exercise judgement in applying Drax's accounting policies to the Target Group. It also requires the use of estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses.

Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis, with revisions recognised in the period in which the estimates are changed and in any future periods affected.

The areas involving a higher degree of judgement or complexity are set out below and in more detail in the related notes.

### **Critical accounting judgements**

The following is the critical judgement, apart from those involving estimation (which are dealt with separately below), made in the process of applying Drax's accounting policies to the historic financial

information of the Target Group that have had the most significant effect on the amounts recognised in the historic financial information:

#### *Asset impairment*

An asset of the Target Group is reviewed for impairment whenever there is an indication that the asset is being carried at more than its recoverable amount. An assessment of whether there is any indication of impairment is made at the end of each reporting period.

For the purpose of this assessment, reflecting the circumstances at the time of the preparation of this Circular, the assets of the Target Group have been treated as forming three distinct cash-generating units (“**CGUs**”) – being the smallest groups of assets considered to generate independent cash flows in their current configuration and operating regime as a standalone group. The three CGUs are: a Hydro CGU (comprising the Cruachan pumped storage hydro and run-of-river hydro locations at Galloway and Lanark), a CCGT CGU (comprising the gas-fired power stations at Shoreham, Damhead Creek, Rye House and Blackburn) and the biomass-from-waste plant at Daldowie.

In preparing the historical financial information, the CCGT and Daldowie CGUs were determined to have been impaired prior to the earliest period presented. The carrying amounts of these CGUs at 1 January 2015 reflect management’s assessment of the recoverable amount of the CGUs.

The estimated present value of future cash flows expected to be derived from the asset, on which the assessment of recoverable amount is based, is inherently dependent upon a number of assumptions. Notably, expected cash flows are based upon management’s assessment of future prices, output, costs, economic support and access to contracts for electricity generation. Where relevant, and to the fullest extent possible, the key assumptions are based on observable market information. However, observable market information is only available for a limited proportion of the remaining useful lives of the assets under review.

#### **Areas of estimation uncertainty**

The areas of estimation uncertainty that carry the most significant risk of an outcome that differs from the amount recognised in the historical information are as follows:

##### *Useful lives of property, plant & equipment*

The useful economic life (“**UEL**”) of the Target Group’s assets is reviewed annually at each balance sheet date, taking into account regulatory change and commercial and technological obsolescence, as well as normal wear and tear (see Note 6).

##### *Pensions*

The Target Group recognises a liability in the combined balance sheet for its obligation to provide benefits under an approved defined benefit pension scheme, less the fair value of any assets held by the pension scheme. The valuation of the scheme assets and liabilities depends on assumptions regarding interest rates, inflation, future pension and salary increases, mortality and other factors, any of which may be subject to future change (see Note 15).

##### *Taxation*

In accounting for both the current and deferred tax obligations of the Target Group, assumptions are made regarding the likely treatment of items of income and expenditure for tax purposes. These assumptions are based on interpretation of relevant legislation and, where required, consultation with external advisers (see Note 5).

## **1. Revenue**

Revenue represents the fair value of the consideration received or receivable for goods or services provided in the normal course of business, net of trade discounts, VAT and other sales-related taxes and excluding transactions between the companies within the Target Group.

Revenues from the sale of electricity are measured based upon metered output delivered at rates specified under contract terms or prevailing market rates as applicable. Revenue from the sale of ROCs is recognised when the ROC is transferred to another party.

Revenues derived from the provision of services (for example, the supply of system support services) are recognised by reference to the stage of completion of the contract.

Fuel sales principally represents the sale of processed fuel pellets. Income is recognised based on the weight of fuel pellets transferred to third parties during the period.

Other income is principally comprised of rebates, which are recognised in the period to which they relate.

An analysis of revenue is provided in the table below. All revenues arose in the United Kingdom.

	Year ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Power Generation</b>			
Electricity sales	519.5	518.2	553.2
ROC sales	6.9	6.5	7.2
Ancillary services	85.3	71.9	93.1
Fuel sales	21.0	19.5	47.4
Other income	8.6	6.3	6.8
<b>Total revenue</b>	<b>641.3</b>	<b>622.4</b>	<b>707.7</b>

Subsequent to the preparation of the historical financial information, on 15 November 2018, the European Commission's State aid approval for the UK Capacity Market was annulled following a ruling of the General Court of the European Union. This ruling prevents the UK Government from holding any capacity auctions or making any capacity payments under existing agreements until re-approval. Further information on the Capacity Market Ruling is set out in sections 3 and 7 of Part I (*Letter from the Chairman of Drax Group plc*).

The Target Group received capacity payments totalling £3.9m in 2017 (2016 and 2015: £nil) included in the table above.

## 2. Segmental reporting

The Target Group is comprised of a single business with a shared management team and trading function. Over the period, the Target Group's activities (the generation of power in the UK) were considered to represent a single operating segment.

## 3. Operating expenses and EBITDA

This note sets out the material components of 'Operating and administrative expenses' in the combined income statement, and the fees the Target Group paid to its auditor, KPMG LLP (in 2017) and EY (in 2016 and 2015), in respect of the services provided to the Target Group over the three-year period.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Gross profit</b>	<b>108.0</b>	<b>105.4</b>	<b>117.8</b>
Staff costs (Note 13)	(22.0)	(20.6)	(20.9)
Repairs & maintenance expenditure	(7.4)	(6.4)	(6.2)
Operating lease rentals	(0.8)	(0.8)	(0.8)
Other operating and administrative expenses	(22.5)	(23.8)	(23.6)
<b>Total operating and administrative expenses</b>	<b>(52.7)</b>	<b>(51.6)</b>	<b>(51.5)</b>
Overhead allocated by Related Parties	(19.2)	(19.5)	(17.5)
<b>EBITDA</b>	<b>36.1</b>	<b>34.3</b>	<b>48.8</b>

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Audit fees:</b>			
Fees payable for the audit of the Target Group's financial statements	0.1	0.1	0.2
<b>Total auditor's remuneration</b>	<b><u>0.1</u></b>	<b><u>0.1</u></b>	<b><u>0.2</u></b>

Overhead allocated by Related Parties reflects costs incurred by Related Parties in respect of services provided and recharged to the Target Group in the period.

#### 4. Net finance costs

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Interest payable and similar charges:</b>			
Interest on borrowings payable to Related Parties	(6.5)	(5.9)	(11.4)
Unwinding of discount on provisions (Note 14)	(0.2)	(0.3)	(0.2)
Net finance cost in respect of defined benefit pension scheme (Note 15)	(0.1)	(0.1)	(0.1)
<b>Total interest payable and similar charges</b>	<b>(6.8)</b>	<b>(6.3)</b>	<b>(11.7)</b>
<b>Interest receivable:</b>			
Interest income on bank deposits	0.1	—	—
<b>Total interest receivable</b>	<b>0.1</b>	<b>—</b>	<b>—</b>
<b>Foreign exchanges losses</b>	<b>—</b>	<b>(0.2)</b>	<b>(0.1)</b>
<b>Net Finance Costs</b>	<b><u>(6.7)</u></b>	<b><u>(6.5)</u></b>	<b><u>(11.8)</u></b>

#### 5. Current and deferred taxation

##### Accounting policy

Taxable profit differs from profit before tax as reported in the combined income statement of the Target Group because it excludes items of income or expense that are either taxable or deductible in other years or never taxable/deductible. The Target Group's liability (or asset) for current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

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

The rate of corporation tax payable in the UK for the year ended 31 December 2017 was 19.25 per cent. (2016: 20 per cent.) (2015: 20.25 per cent.). The UK main rate of corporation tax is set at 19 per cent. for the years starting 1 April 2018 and 2019, and 17 per cent. for the year starting 1 April 2020. These rates will apply to the tax payable by the Target Group in those periods and also impact on the deferred tax balances in this historical financial information.

In accounting for taxation the Target Group makes assumptions regarding the treatment of items of income and expenditure for tax purposes. The Target Group believes that the assumptions are reasonable based on prior experience and consultation with advisers. Full provision is made for deferred taxation at the rates of tax prevailing at the period end date unless future rates have been substantively enacted. Deferred tax assets are recognised where it is considered more likely than not that they will be recovered.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Tax credit/(charge) comprises:</b>			
Current tax	1.2	2.1	4.4
Deferred tax			
- Before impact of corporation tax rate change	(3.7)	(6.1)	(6.5)
- Impact of corporation tax rate change	3.5	3.2	6.4
<b>Tax credit/(charge)</b>	<b>1.0</b>	<b>(0.8)</b>	<b>4.3</b>
<b>Tax credit/(charge) for items recognised in other comprehensive income:</b>			
Deferred tax on actuarial losses	0.4	0.4	—
Deferred tax on cash flow hedges	—	(0.6)	0.2
<b>Tax credit/(charge) in other comprehensive income</b>	<b>0.4</b>	<b>(0.2)</b>	<b>0.2</b>

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Profit before tax</b>	<b>12.8</b>	<b>12.1</b>	<b>5.2</b>
Profit before tax multiplied by the rate of corporation tax in the UK of 19.25% (2016: 20%) (2015: 20.25%)	(2.5)	(2.4)	(1.0)
<b>Effects of:</b>			
Expenses not deductible for tax purposes	—	(0.5)	(0.2)
Impact of change to corporation tax rate	3.5	3.2	6.4
Other	—	(1.1)	(0.9)
<b>Total tax credit/(charge)</b>	<b>1.0</b>	<b>(0.8)</b>	<b>4.3</b>

#### Deferred tax (liabilities)/assets

	Capital Allowances £m	Derivatives £m	Pensions £m	Other £m	Total £m
At 1 January 2015	(1.2)	(2.3)	1.3	0.2	(2.0)
Charged/credited to income statement	(2.7)	2.8	(0.1)	(0.1)	(0.1)
Charged credited to other comprehensive income	—	0.2	—	—	0.2
At 1 January 2016	(3.9)	0.7	1.2	0.1	(1.9)
Charged/credited to income statement	(2.7)	—	(0.2)	—	(2.9)
Charged credited to other comprehensive income	—	(0.6)	0.4	—	(0.2)
At 1 January 2017	(6.6)	0.1	1.4	0.1	(5.0)
Charged/credited to income statement	—	—	(0.2)	—	(0.2)
Charged credited to other comprehensive income	—	—	0.4	—	0.4
<b>At 31 December 2017</b>	<b>(6.6)</b>	<b>0.1</b>	<b>1.6</b>	<b>0.1</b>	<b>(4.8)</b>

## 6. Property, plant and equipment

This note shows the cost, depreciation and net book value of the physical assets controlled by the Target Group that are used to generate revenue.

#### Accounting policy

Property, plant and equipment are initially measured at cost. Cost comprises the purchase price and directly attributable costs of bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Property, plant and equipment are stated at cost less accumulated depreciation and any provision for impairment in value.

Depreciation is provided on a straight-line basis to write down assets to their residual value evenly over the estimated useful lives of the assets from the date of acquisition. An asset's net book value is its cost less any depreciation (including impairment, if required) charged to date.

The table below shows the range of useful lives applied at the purchase date and the average remaining useful life of an asset in the main categories of asset the Target Group owns in years:

	Average remaining UEL (range at purchase date)
Buildings	14
Hydro-electric plant	14 (4-105)
Gas-fired plant	17 (2-40)
Other plant & equipment	3 (4-12)

Freehold land, held at cost, is considered to have an unlimited useful life and is not depreciated.

The assets' residual value, useful lives and depreciation methods are reviewed and adjusted prospectively if appropriate, or if there is an indication of a significant change since the last reporting date.

	Hydro Plant £m	Gas Plant £m	Other Plant £m	Assets under Construction £m	Total £m
<b>Cost:</b>					
At 1 January 2015	148.0	939.9	144.0	33.1	1,265.0
Additions at cost	—	1.2	1.6	23.5	26.3
Disposals	(0.1)	(38.0)	(0.5)	(2.6)	(41.2)
Issues/transfers	2.4	20.2	0.1	(22.7)	—
At 1 January 2016	150.3	923.3	145.2	31.3	1,250.1
Additions at cost	—	1.1	1.5	17.6	20.2
Disposals	—	(2.5)	(8.2)	(0.5)	(11.2)
Issues/transfers	2.3	11.5	—	(13.8)	—
At 1 January 2017	152.6	933.4	138.5	34.6	1,259.1
Additions at cost	—	0.4	1.6	20.1	22.1
Disposals	—	(19.3)	(0.2)	(0.6)	(20.1)
Issues/transfers	4.6	20.3	(0.1)	(25.3)	(0.5)
At 31 December 2017	157.2	934.8	139.8	28.8	1,260.6
<b>Accumulated depreciation:</b>					
At 1 January 2015	78.2	875.5	50.4	—	1,004.1
Charge for the year	4.4	8.2	3.9	—	16.5
Disposals	(0.1)	(36.8)	(0.3)	—	(37.2)
At 1 January 2016	82.5	846.9	54.0	—	983.4
Charge for the year	4.8	6.6	2.9	—	14.3
Disposals	—	(2.5)	(6.5)	—	(9.0)
At 1 January 2017	87.3	851.0	50.4	—	988.7
Charge for the year	4.7	8.7	3.3	—	16.7
Issues/transfers	(0.3)	—	—	—	(0.3)
Disposals	—	(18.7)	—	—	(18.7)
At 31 December 2017	91.7	841.0	53.7	—	986.4
<b>Net book amount at 31 December 2015</b>	<b>67.8</b>	<b>76.4</b>	<b>91.2</b>	<b>31.3</b>	<b>266.7</b>
<b>Net book amount at 31 December 2016</b>	<b>65.3</b>	<b>82.4</b>	<b>88.1</b>	<b>34.6</b>	<b>270.4</b>
<b>Net book amount at 31 December 2017</b>	<b>65.5</b>	<b>93.8</b>	<b>86.1</b>	<b>28.8</b>	<b>274.2</b>

## 7. Intangible assets

Intangible assets are comprised of computer software controlled by the Target Group.

## Accounting policy

Computer software assets are measured at cost. Cost comprises the purchase price (net of any discount or rebate) and any directly attributable costs in bringing the asset into the condition and use required for use as intended by management. Software assets are amortised to the income statement on a straight-line basis over periods of up to five years.

	Computer Software £m
<b>Cost:</b>	
At 1 January 2015	7.8
Additions at cost	0.2
Disposals	—
At 1 January 2016	8.0
Additions at cost	0.9
Disposals	(0.4)
At 1 January 2017	8.5
Additions at cost	0.3
Transfer from property, plant & equipment	0.5
At 31 December 2017	9.3
<b>Accumulated depreciation:</b>	
At 1 January 2015	6.5
Charge for the year	0.6
Disposals	—
At 1 January 2016	7.1
Charge for the year	0.5
Disposals	(0.3)
At 1 January 2017	7.3
Charge for the year	0.7
Transfer from property, plant & equipment	0.3
At 31 December 2017	8.3
<b>Net book amount at 31 December 2015</b>	<b>0.9</b>
<b>Net book amount at 31 December 2016</b>	<b>1.2</b>
<b>Net book amount at 31 December 2017</b>	<b>1.0</b>

## 8. Trade and other receivables

Trade receivables represent amounts owed to the Target Group by customers for goods or services provided but not yet paid for. Other receivables include accrued income, which is income earned in the period but not yet invoiced, largely in respect of electricity delivered that will be invoiced the following month, and prepayments, which are amounts paid by the Target Group for which the relevant goods or services are yet to be received or utilised.

### Accounting policy

Trade and other receivables that have no stated interest rate and are due to be settled within one year are initially and subsequently measured at the undiscounted amount of consideration expected to be received, net of impairment.

Trade and other receivables that have a stated interest rate are initially measured at the transaction price. Subsequently, such instruments are measured at amortised cost using the effective interest method.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<i>Amounts falling due within one year:</i>			
Trade receivables	8.0	9.4	6.3
Accrued income	11.0	5.6	8.3
Prepayments and other receivables	1.7	3.0	3.4
<b>External trade &amp; other receivables</b>	<b>20.7</b>	<b>18.0</b>	<b>18.0</b>
Amounts due from Related Parties	117.0	98.5	104.9
<b>Total trade &amp; other receivables</b>	<b>137.7</b>	<b>116.5</b>	<b>122.9</b>

Amounts due from Related Parties reflect amounts receivable from other companies within the Iberdrola group principally in respect of sales of electricity and ROCs.

Trade receivables and accrued income are stated net of a provision for impairment of doubtful debts totalling £6.3 million (2016: £4.4 million) (2015: £1.7 million). The credit risk of the Target Group relates to counterparties in the energy industry or financial institutions operating in energy markets. The carrying amount of receivables represents the maximum exposure of the Target Group to credit risk.

## 9. Trade and other payables

Trade and other payables represent amounts owed to suppliers (for goods and services provided), tax authorities and other creditors that are due to be paid in the ordinary course of business.

The Target Group makes accruals for amounts that will fall due for payment in the future as a result of its current activities.

### Accounting policy

Trade and other payables that have no stated interest rate and are due to be settled within one year are initially and subsequently measured at the undiscounted amount of consideration expected to be received.

Trade and other payables that have a stated interest rate are initially measured at the transaction price. Subsequently, such instruments are measured at amortised cost using the effective interest method.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<i>Amounts falling due within one year:</i>			
Fuel accruals	0.1	0.1	0.1
Trade payables	5.7	7.4	8.2
Other taxes & social security	16.7	19.9	12.1
Capital payables and accruals	5.2	4.6	5.6
Other payables	1.5	1.6	2.4
<b>External trade &amp; other payables</b>	<b>29.2</b>	<b>33.6</b>	<b>28.4</b>
Amounts due to related parties	113.6	66.4	113.2
<b>Total trade &amp; other payables</b>	<b>142.8</b>	<b>100.0</b>	<b>141.6</b>
<i>Amounts falling due after more than one year:</i>			
<b>Deferred income</b>	<b>0.3</b>	<b>0.4</b>	<b>0.5</b>



## 10. Borrowings from related parties

The Target Group has historically been funded by borrowings from Related Parties. The amounts outstanding under such arrangements are shown in the table below.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Falling due within one year	402.4	520.3	437.0
Falling due after more than one year	100.0	—	—
<b>Total borrowings</b>	<b>502.4</b>	<b>520.3</b>	<b>437.0</b>

Amounts falling due within one year attract a variable interest rate of base rate plus 1 per cent. and are repayable on demand.

Amounts falling due after more than one year attract a fixed interest rate of 2.66 per cent. and have fixed repayment dates in 2027.

Related party borrowings will be settled as part of the transaction. There are no external borrowings in the Target Group.

## 11. Inventory

Inventory reflects the cost of fuel pellets produced at the Target Group's biomass-from-waste plant but not yet sold.

## 12. Cash generated from operations

This note shows adjustments for any non-cash accounting items in the combined income statement and changes in working capital to reconcile net profit for the year to the amount of cash generated from the Target Group's operations.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
<b>Profit for the year</b>	<b>13.8</b>	<b>11.3</b>	<b>9.5</b>
Adjustments for:			
Interest payable and similar charges	6.8	6.5	11.8
Interest receivable	(0.1)	—	—
Taxation	(1.0)	0.8	(4.3)
Depreciation	16.7	14.3	16.5
Amortisation	0.7	0.5	0.6
Gains on disposal	(1.6)	—	(0.3)
Asset obsolescence charges	0.8	0.9	0.8
Unrealised losses on derivative contracts	—	—	14.2
Defined benefit current service cost	2.9	2.6	2.8
Change in provisions	0.2	1.0	(0.2)
<b>Operating cash flows before movement in working capital</b>	<b>39.2</b>	<b>37.9</b>	<b>51.4</b>
<b>Changes in working capital:</b>			
Receivables	(21.3)	6.4	(5.5)
Payables	41.1	(30.6)	(92.8)
Inventories	(0.1)	(0.2)	0.1
<b>Total Increase / Decrease in Working Capital</b>	<b>19.7</b>	<b>(24.4)</b>	<b>(98.2)</b>
Defined benefit pension contributions	(4.5)	(3.3)	(3.4)
Provisions paid	(0.2)	(1.2)	(0.5)
<b>Cash generated from/(absorbed by) operations</b>	<b>54.2</b>	<b>9.0</b>	<b>(50.7)</b>

### 13. Employees

This note provides a breakdown of the cost of the Target Group's employees. The average number of employees is also provided.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Wages & salaries	17.6	17.2	17.3
Social security costs	1.8	1.8	1.7
Pension costs	3.6	3.0	3.3
Less capitalised staff costs	(1.0)	(1.4)	(1.4)
	<b>22.0</b>	<b>20.6</b>	<b>20.9</b>

#### Average monthly number of people employed

	Years ended 31 December		
	2017 (number)	2016 (number)	2015 (number)
Operations	254	258	259
Administrative services	26	26	27
	<b>280</b>	<b>284</b>	<b>286</b>

The note above does not reflect the number of employees that will transfer upon completion of the transaction.

### 14. Provisions

#### Accounting policy

Provisions are recognised where the Target Group has a legal or constructive present obligation as a result of a past event, it is probable that the Target Group will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

Specifically, provision is made for the estimated decommissioning costs at the end of the useful economic life of the Target Group's gas-fired generating assets. Decommissioning provisions are not made in respect of the hydro assets nor the biomass-from-waste facility. The remaining life of the hydro assets is too long to be able to reliably estimate the cost of decommissioning and following the effects of discounting, the amount is not expected to be material.

The amount provided represents the present value of the expected costs. The discount rate used is a risk-free pre-tax rate of 1.8 per cent., reflecting the fact that the estimated future cash flows have built-in risks specific to the liability.

	Decommissioning £m	Other £m	Total £m
Carrying amount at 1 January 2015	8.7	0.9	9.6
Additions	1.5	0.2	1.7
Adjustment for changes in assumptions	—	—	—
Unwinding of discount	0.2	—	0.2
Utilisation	—	(0.5)	(0.5)
Released	—	(0.4)	(0.4)
Carrying amount at 1 January 2016	10.4	0.2	10.6
Additions	1.1	1.0	2.1
Adjustment for changes in assumptions	—	—	—
Unwinding of discount	0.3	—	0.3
Utilisation	—	(1.2)	(1.2)
Released	—	—	—
Carrying amount at 1 January 2017	11.8	—	11.8
Additions	0.4	0.2	0.6
Adjustment for changes in assumptions	—	—	—
Unwinding of discount	0.2	—	0.2
Utilisation	(0.2)	—	(0.2)
Released	—	—	—
<b>Carrying amount at 31 December 2017</b>	<b>12.2</b>	<b>0.2</b>	<b>12.4</b>

## 15. Retirement benefit obligations

### Defined contribution scheme

The Target Group operates a defined contribution pension scheme. Pension costs for the defined contribution scheme are as follows:

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Total contributions to defined contribution pension schemes included in staff costs	<u>0.4</u>	<u>0.5</u>	<u>0.4</u>

### Defined benefit scheme

The Target Group participates in a defined benefit pension scheme, the ScottishPower Pension Scheme (“SPPS”). The SPPS is closed to new entrants. Members who joined prior to this closure continue to accrue benefits as part of the scheme.

The Target Group has not previously calculated its share of the SPPS assets and obligation separately. For the purpose of this historical financial information, an exercise has been undertaken by a qualified actuary to establish the Target Group’s allocation of the scheme assets and its liabilities as at 31 December 2017 on a basis proportionate to the participation of the Target Group’s employees in the overall scheme. The information for 2016 and 2015 has been calculated in a manner consistent with this assessment, as noted in the Basis of preparation.

Since the amounts relating to the Target Group are based on an allocation of the SPPS assets and liabilities, certain disclosures (including a breakdown of the nature of the scheme assets and a sensitivity analysis to the key assumptions) have not been provided.

The principal assumptions applied in measuring the present value of the defined benefit obligation, were as follows:

### Assumptions

	Years ended 31 December		
	2017 %	2016 %	2015 %
Discount rate	2.6	2.9	3.8
Inflation	3.2	3.0	3.1
Rate of increase deferred pensions	3.2	3.0	3.1
Rate of increase in pensions payments	3.1	2.9	3.0
Rate of increase in pensionable salaries	3.7	3.5	3.6

### Balance Sheet Liability

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Allocated share of defined benefit obligation	(71.6)	(68.6)	(59.9)
Allocated share of fair value of plan assets	65.0	62.7	55.3
<b>Net liability recognised in the balance sheet</b>	<b>(6.6)</b>	<b>(5.9)</b>	<b>(4.6)</b>

### Amounts recognised in the income statement

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Allocated share of current service cost (in staff costs)	2.9	2.6	2.8
Allocated share of interest on net defined benefit liability (in net interest costs)	0.1	0.1	0.1
<b>Total amounts recognised in income statement</b>	<b>3.0</b>	<b>2.7</b>	<b>2.9</b>

### Actuarial losses

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Cumulative actuarial losses at 1 January	(1.8)	0.1	—
Actuarial losses recognised in other comprehensive income in the year	(2.2)	(1.9)	0.1
<b>Cumulative actuarial losses at 31 December</b>	<b>(4.0)</b>	<b>(1.8)</b>	<b>0.1</b>

### Changes in present value of defined benefit obligation

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Allocated share of defined benefit obligation at 1 January	68.6	59.9	59.9
Current service cost	2.9	2.6	2.8
Employee contributions	0.1	0.1	0.1
Interest cost	0.1	0.1	0.1
Actuarial losses/(gains)	4.5	9.6	(0.6)
Benefits paid	(4.6)	(3.7)	(2.4)
<b>Allocated share of defined benefit obligation at 31 December</b>	<b>71.6</b>	<b>68.6</b>	<b>59.9</b>

## Changes in fair value of plan assets

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Allocated share of fair value of plan assets at 1 January	62.7	55.3	54.7
Interest income on plan assets	—	—	—
Employee contributions	0.1	0.1	0.1
Employer contributions	4.5	3.3	3.4
Remeasurement gains/(losses)	2.3	7.7	(0.5)
Benefits paid	(4.6)	(3.7)	(2.4)
<b>Allocated share of fair value of plan assets at 31 December</b>	<b><u>65.0</u></b>	<b><u>62.7</u></b>	<b><u>55.3</u></b>

## 16. Risk management disclosures

### Capital and liquidity risk

The capital structure of the Target Group consists of borrowings from Related Parties (including current and non-current interest-bearing loans as shown in Note 10).

Funding and liquidity requirements have historically been managed centrally by a Related Party, through the issue or repayment of related party borrowings.

### Commodity price risk

The Target Group is potentially exposed to the effect of fluctuations in commodity prices, particularly the price of electricity and the price of gas. Historically, this exposure has been managed by a Related Party.

The Target Group has historically sold all of its output to, and procured all of its commodities from, related parties at prices reflecting the price achieved by the related party in the relevant market. Accordingly, the results of the Target Group over the period presented reflect fluctuations in commodity prices over the period after taking into account these risk management activities undertaken by a Related Party.

### Foreign currency, interest and credit risk

Owing to the central management of these risks within the Iberdrola group, the Target Group has not historically been materially exposed to foreign currency, interest or credit risk. The maximum extent of credit risk faced by the Target Group is reflected in the carrying amount of receivables shown in Note 8.

## 17. Financial instruments

### Derivative financial instruments

The Target Group holds a small number of foreign currency forward purchase contracts for the purpose of securing the sterling cost of purchases denominated in a currency other than sterling.

These contracts are recognised in the balance sheet and measured at fair value. The contracts are designated into hedge accounting relationships in accordance with IFRS and, accordingly, changes in the fair value of the contracts during each period are recognised as a component of other comprehensive income.

Historically, the Target Group has used forward purchase contracts to secure the price of gas purchases. The unwind of the last of these arrangements can be seen in the income statement in 2015 (unrealised losses of £14.2 million).

### Other financial instruments

The Target Group holds a variety of non-derivative financial instruments, including amounts due from and owing to Related Parties, and trade payables and receivables arising from operations.

Trade and other receivables (Note 8) and trade and other payables (Note 9) generally have short times to maturity. For this reason, their carrying values, on the amortised cost basis, approximate to their fair value.

## 18. Commitments

The Target Group has a number of financial commitments (i.e. a contractual requirement to make a cash payment in the future) that are not recorded in the balance sheet as the contract is not yet due for delivery.

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Contracts placed for future capital expenditure not provided in the financial statements	2.1	1.3	1.2
Future commitments under support contracts	13.7	10.8	15.2
	<b>15.8</b>	<b>12.1</b>	<b>16.4</b>

The contractual maturity of future commitments is as follows:

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Within one year	13.2	11.1	14.2
Between two to five years	2.6	1.0	2.2
	<b>15.8</b>	<b>12.1</b>	<b>16.4</b>

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Within one year	0.7	0.9	0.8
Within two to five years	2.8	3.5	2.9
After five years	11.8	6.4	6.4
	<b>15.3</b>	<b>10.8</b>	<b>10.1</b>

## 19. General information

ScottishPower Generation Limited, registered company number SC189124, is a private company limited by shares incorporated in Scotland. Its registered address is 320 St. Vincent Street, Glasgow G2 5AD.

ScottishPower Generation Limited and its subsidiary have one principal activity: the supply of energy in the United Kingdom.

The subsidiary of ScottishPower Generation Limited at 31 December 2017 was:

<u>Name</u>	<u>Country of Incorporation</u>	<u>Class of Shares</u>	<u>Holding</u>	<u>Principal activity</u>
SMW Limited	Scotland	Ordinary	100%	Production of fuel pellets

## 20. New accounting standards

As at the date of the most recent balance sheet included in this historical financial information, certain new or amended accounting standards, which have not been applied in the preparation of this historical financial information, were in issue but not yet effective.

### **A listing of new standards, interpretations and pronouncements which are in issue but not yet effective**

IFRS 2 – Classification and Measurement of Share-based Payment Transactions – effective for annual periods beginning on or after 1 January 2018

IFRS 9 – Financial Instruments – effective for annual periods beginning on or after 1 January 2018

IFRS 15 – Revenue from Contracts with Customers – effective for annual periods beginning on or after 1 January 2018

IAS 40 (amended) – Investment Property – effective for annual periods beginning on or after 1 January 2018

IFRIC 22 – Foreign Currency Transactions and Advance Consideration – effective for annual periods beginning on or after 1 January 2018

IFRIC 23 – Uncertainty over Income Tax Treatments – effective for annual periods beginning on or after 1 January 2019

IFRS 16 – Leases – effective for annual periods beginning on or after 1 January 2019

IFRS 10 (amended) – Consolidated Financial Statements, and IAS 28 (amended) – Investments in Associates and Joint Ventures (2011) – effective date deferred indefinitely

Adoption of the above standards in future periods is not expected to have a material impact on the financial statements of the Target Group at 31 December 2017.

### **IFRS 16 – Leases**

IFRS 16 introduces a new model for accounting for leases. The principal change compared to the current standard (IAS 17 – Leases) is to record leases previously classified as operating leases in the balance sheet, subject to exemptions and exceptions for short-term and low-value leases.

The Target Group's principal leases relate to property, plant and equipment. Most of these leases are classified as operating leases under IAS 17. The Target Group expects to recognise 'right-of-use' assets and corresponding liabilities, where the Target Group is a lessee.

The precise effect of the above change on the Target Group's balance sheet and income statement has not yet been quantified. At 31 December 2017, the Target Group had non-cancellable operating lease commitments of £15.3 million.

## **21. Related party transactions**

A related party is either an individual with control or significant influence over the Target Group, or a company that is linked to the Target Group by investment (i.e. another company ultimately owned and controlled by Iberdrola S.A., associate or joint venture) or a related individual (i.e. an individual with significant influence or control over both entities).

The Target Group's principal related parties are other entities ultimately owned by Iberdrola S.A. Throughout this historical financial information, references to transactions or balances with Related Parties refer to any transaction or balance with another entity ultimately owned and controlled by Iberdrola S.A.

### **Entities with significant influence over the Target Group**

At 31 December 2017, SPGEN and SMW were wholly owned subsidiaries of Iberdrola S.A. The ultimate controlling party was Iberdrola S.A.

### **Purchases from related parties**

Historically the Target Group has procured all of its commodity requirements from Related Parties at prices reflecting the value achieved by the relevant related party with an external counterparty.

The value of purchases during each period amounted to £456.6 million, £429.0 million and £495.9 million for 2017, 2016 and 2015 respectively. The amount payable in respect of these purchases at 31 December 2017, 2016 and 2015 is shown in Note 9 as amounts due to Related Parties.

### **Sales to related parties**

Historically the Target Group has sold all of its electrical output and ROCs to Related Parties, at prices reflecting the value achieved by the relevant related party with an external counterparty.

The value of sales during each period amounted to £535.0 million, £531.7 million and £593.7 million for 2017, 2016 and 2015 respectively. The amount receivable in respect of these sales at 31 December 2017, 2016 and 2015 is shown in Note 8 as amounts receivable from Related Parties.

### Commitments with related parties

Of the commitments shown in Note 18, £nil were with Related Parties (2016: £nil) (2015: £0.1 million).

### Transactions with key management personnel

The remuneration of the key management personnel of the Target Group, is set out below in aggregate for each of the categories specified in IAS 24 (Related Party Disclosures).

	Years ended 31 December		
	2017 £m	2016 £m	2015 £m
Salaries and short-term benefits	1.2	1.4	1.1
Aggregate amounts receivable under shared-based incentive schemes	0.5	0.4	0.4
Employer contributions to pension schemes	0.2	0.3	0.2
	<b>1.9</b>	<b>2.1</b>	<b>1.7</b>

All of the key management personnel of the Target Group were remunerated for their work on behalf of Related Parties in addition to the Target Group. Their remuneration, shown in the table above, is not apportioned for their work specifically in respect of the Target Group, and includes amounts paid by Related Parties. Of the nine (2016: ten) (2015: eight) key management personnel of the Target Group, two (2016: four) (2015: one) were paid directly by the Target Group.

Amounts included in the table above reflect the remuneration of two (2016: two) (2015: two) members of the board of directors of SPGEN in the relevant period.

The highest paid director of SPGEN received remuneration of £602,000 (2016: £615,000) (2015: £489,000). The value of the Target Group's contributions paid to a defined contribution pension scheme in respect of the highest paid director amount to £92,000 (2016: £85,000) (2015: £77,000).



**Part B: Accountant's Report on Historical Financial Information relating to the ScottishPower Generation Group**

**Deloitte.**

Deloitte LLP  
1 New Street Square  
London  
EC4A 3HQ

The Board of Directors  
on behalf of Drax Group plc  
Drax Power Station  
Selby  
North Yorkshire  
YO8 8PH

J.P. Morgan Securities  
25 Bank Street  
Canary Wharf  
London  
E14 5JP

5 December 2018

Dear Sirs

**ScottishPower Generation Group (the "Target Group")**

We report on the financial information for the 3 years ending 31 December 2017 set out in Part V of the Class 1 Circular relating to the acquisition of the Target Group dated 5 December 2018 by Drax Group plc (the "Company" and, together with its subsidiaries, the "Group") (the "Circular"). This financial information has been prepared for inclusion in the Circular on the basis of the accounting policies and basis of preparation set out in the financial information. This report is required by Listing Rule 13.5.21R and is given for the purpose of complying with that requirement and for no other purpose.

**Responsibilities**

As described in paragraph I Part VIII the Directors of the Company are responsible for preparing the financial information on the basis of preparation set out in the accounting policies.

It is our responsibility to form an opinion on the financial information and to report our opinion to you.

Save for any responsibility which we may have to those persons to whom this report is expressly addressed and which we may have as a result of the inclusion of this report in the Circular, to the fullest extent permitted by law we do not assume any responsibility and will not accept any liability to any other person for any loss suffered by any such other person as a result of, arising out of, or in connection with this report or our statement, required by and given solely for the purposes of complying with Listing Rule 13.4.1R(6), consenting to its inclusion in the Circular.

**Basis of opinion**

We conducted our work in accordance with Standards for Investment Reporting issued by the Auditing Practices Board in the United Kingdom. Our work included an assessment of evidence relevant to the amounts and disclosures in the financial information. It also included an assessment of significant estimates and judgments made by those responsible for the preparation of the financial information and whether the accounting policies are appropriate to the entity's circumstances, consistently applied and adequately disclosed.

We planned and performed our work 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 information is free from material misstatement whether caused by fraud or other irregularity or error.

Our work has not been carried out in accordance with auditing or other standards and practices generally accepted in jurisdictions outside the United Kingdom, including the United States of America, and accordingly should not be relied upon as if it had been carried out in accordance with those standards and practices.

### **Opinion on financial information**

In our opinion, the financial information gives, for the purposes of the Circular, a true and fair view of the state of affairs of the Target Group as at 31 December 2015, 2016 and 2017 and of its profits, cash flows and changes in equity for the 3 years ending 31 December 2015, 2016 and 2017 in accordance with the basis of preparation set out in the financial information and has been prepared in a form that is consistent with the accounting policies adopted in the Company's latest annual accounts.

Yours faithfully

Deloitte LLP

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**PART VI**  
**UNAUDITED PRO FORMA FINANCIAL INFORMATION**  
**RELATING TO THE ENLARGED GROUP**

**Part A: Unaudited pro forma financial information**

The unaudited pro forma income statement and unaudited pro forma net assets statement of the Enlarged Group (together the “**Unaudited Pro Forma Financial Information**”) set out in Part A in this Part VI (*Unaudited Pro Forma Financial Information relating to the Enlarged Group*) has been prepared on the basis of the notes below, and in accordance with Listing Rule 13.3.3R, to illustrate the impact of the Acquisition on the income statement of Drax Group plc for the year ended 31 December 2017, as if it had taken place on 1 January 2017, and on the net assets of Drax Group plc as at 31 December 2017, as if it had taken place at that date.

The Unaudited Pro Forma Financial Information has been prepared on a basis consistent with the accounting policies and presentation adopted by Drax Group plc in relation to its consolidated financial statements for the year ended 31 December 2017 and includes the combined income statement of the ScottishPower Generation Group for the year ended 31 December 2017 and net assets of the ScottishPower Generation Group as at 31 December 2017.

The Unaudited Pro Forma Financial Information has been prepared for illustrative purposes only and, by its nature, addresses a hypothetical situation and does not, therefore, represent the Enlarged Group’s actual financial position or results. The Unaudited Pro Forma Financial Information does not purport to represent what the Enlarged Group’s financial position and results of operations actually would have been if the Acquisition had been completed on the dates indicated, nor does it purport to represent the results of operations for any future period or the financial condition at any future date.

The Unaudited Pro Forma Financial Information does not constitute financial statements within the meaning of section 434 of the Companies Act 2006. Shareholders should read the whole of this Circular and not rely solely on the summarised financial information contained in this Part VI (*Unaudited Pro Forma Financial Information relating to the Enlarged Group*).

## Part 1 Unaudited Pro Forma Statement of Net Assets

	<i>Adjustments</i>			
	Drax Group plc at 31 December 2017 £m (Note 1)	ScottishPower Generation Group at 31 December 2017 £m (Note 2)	Adjustments £m (Note 3)	Pro forma net assets at 31 December 2017 £m
<b>Assets</b>				
<b>Non-current assets</b>				
Goodwill and other intangible assets	401.9	1.0	—	402.9
Property, plant and equipment	1,661.9	274.2	456.8	2,392.9
Other fixed asset investments	1.3	—	—	1.3
Deferred tax assets	22.7	—	—	22.7
Derivative financial instruments	190.7	0.3	—	191.0
	<u>2,278.5</u>	<u>275.5</u>	<u>456.8</u>	<u>3,010.8</u>
<b>Current assets</b>				
Inventories	272.1	1.0	—	273.1
ROC and LEC assets	145.5	—	—	145.5
Trade and other receivables	417.5	20.7	—	438.2
Amounts receivable from Related Parties	—	117.0	(117.0)	—
Derivative financial instruments	175.5	—	—	175.5
Cash and cash equivalents	222.3	—	—	222.3
Current tax assets	6.2	1.3	—	7.5
	<u>1,239.1</u>	<u>140.0</u>	<u>(117.0)</u>	<u>1,262.1</u>
<b>Total assets</b>	<u><u>3,517.6</u></u>	<u><u>415.5</u></u>	<u><u>339.8</u></u>	<u><u>4,272.9</u></u>
<b>Liabilities</b>				
<b>Current liabilities</b>				
Trade and other payables	736.5	29.2	—	765.7
Amounts payable to Related Parties	—	113.6	(113.6)	—
Borrowings	18.6	—	—	18.6
Borrowings from Related Parties	—	402.4	(402.4)	—
Derivative financial instruments	109.6	—	—	109.6
Provisions	—	0.4	—	0.4
	<u>864.7</u>	<u>545.6</u>	<u>(516.0)</u>	<u>894.3</u>
<b>Net current assets / (liabilities)</b>	374.4	(405.6)	399.0	367.8
<b>Non-current liabilities</b>				
Trade and other payables	—	0.3	—	0.3
Borrowings	571.1	—	723.2	1,294.3
Borrowings from Related Parties	—	100.0	(100.0)	—
Derivative financial instruments	94.2	—	—	94.2
Provisions	36.3	12.0	—	48.3
Deferred tax liabilities	230.0	4.8	—	234.8
Retirement benefit obligations	1.2	6.6	—	7.8
	<u>932.8</u>	<u>123.7</u>	<u>623.2</u>	<u>1,679.7</u>
<b>Total liabilities</b>	<u>1,797.5</u>	<u>669.3</u>	<u>107.2</u>	<u>2,574.0</u>
<b>Net assets / (liabilities)</b>	<u><u>1,720.1</u></u>	<u><u>(253.8)</u></u>	<u><u>232.6</u></u>	<u><u>1,698.9</u></u>

## Notes

No adjustment has been made to reflect any synergies that may arise after the transaction has completed.

No adjustment has been made to reflect the financial results of Drax Group plc or the ScottishPower Generation Group since 31 December 2017.

- (1) The net assets of Drax Group plc as at 31 December 2017 have been extracted without adjustment from the audited consolidated financial statements for the year ended 31 December 2017.
- (2) The net assets of the ScottishPower Generation Group have been extracted without adjustment from the historical financial information included in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) of this Circular.
- (3) The Unaudited Pro Forma Statement of Net Assets has been prepared on the basis that the transaction will be treated as a business combination in accordance with IFRS 3. However, it does not reflect any fair value adjustments to the acquired assets and liabilities, as the fair value measurement of these items will only be performed at the date of Completion. The fair value adjustments, when finalised, may be material. For the purpose of the pro forma statement of net assets, the excess purchase consideration over the carrying amount of net assets of £456.8 million has been attributed to property, plant & equipment.

The preliminary uplift in the value of property, plant & equipment has been calculated as follows:

	£m	£m
Total consideration paid		702.0
Net liabilities of the ScottishPower Generation Group		<u>(253.8)</u>
Purchase consideration in excess of net liabilities		<u>955.8</u>
Adjustments for Related Party balances to be settled as part of the transaction:		
- Amounts receivable from Related Parties	117.0	
- Amounts payable to Related Parties	(113.6)	
- Related Party borrowings	<u>(502.4)</u>	
		<u>(499.0)</u>
Preliminary uplift in value of Property, plant & equipment		<u><u>456.8</u></u>

Upon completion of the Acquisition, the Drax Group will draw down on an acquisition bridge facility with a maximum value of £725 million. For the purpose of the pro forma statement of net assets, the entire purchase price of £702 million plus estimated acquisition-related costs of £23 million have been funded by the acquisition bridge facility. Drax may use available cash reserves to reduce the amount drawn on completion.

The acquisition-related costs are not included in the calculation of the preliminary uplift as they will be expensed as transaction costs or capitalised as borrowing costs, as required by IFRS.

£18 million of the acquisition-related costs are expected to be directly attributable to the purchase of the ScottishPower Generation Group. These costs will be expensed in the income statement.

£5 million of the acquisition-related costs are expected to be directly attributable to the acquisition bridge facility. These costs will be capitalised and offset against total borrowings and are expected to be amortised over the 19-month term of the bridge facility as required by IFRS. This increases interest payable by £3.2 million (being 12/19 months' amortisation of these costs) and reduces borrowings by £1.8 million in the pro forma statements.

## Part 2 Unaudited Pro Forma Income Statement of the Enlarged Group

	Drax Group plc for the year ended 31 December 2017 £m (Note 1)	Adjustments		Pro forma Enlarged Group £m
		ScottishPower Generation Group for the year ended 31 December 2017 £m (Note 2)	Adjustments £m (Note 3)	
Revenue	3,685.2	641.3	—	4,326.5
Fuel costs in respect of generation	(1,356.8)	(294.8)	—	(1,651.6)
Cost of power purchases	(974.6)	—	—	(974.6)
Grid Charges	(498.7)	(36.7)	—	(535.4)
Other energy supply costs	(310.1)	(201.8)	—	(511.9)
Total cost of sales	(3,140.2)	(533.3)	—	(3,673.5)
<b>Gross profit</b>	545.0	108.0	—	653.0
Operating and administrative expenses	(316.1)	(52.7)	—	(368.8)
Overheads allocated by Related Parties	—	(19.2)	—	(19.2)
<b>EBITDA</b>	228.9	36.1	—	265.0
Depreciation and amortisation	(166.3)	(17.4)	—	(183.7)
Asset obsolescence charges	—	(0.8)	—	(0.8)
Other losses	(0.4)	—	—	(0.4)
Acquisition – related costs	(7.8)	—	(18.0)	(25.8)
(Loss)/gain on disposal	(15.4)	1.6	—	(13.8)
Unrealised gains on derivative contracts	(156.1)	—	—	(156.1)
<b>Operating (loss)/profit</b>	(117.1)	19.5	(18.0)	(115.6)
Interest payable and similar charges	(66.3)	(6.8)	(29.8)	(102.9)
Interest receivable	0.2	0.1	—	0.3
<b>(Loss)/Profit before tax</b>	(183.2)	12.8	(47.8)	(218.2)
Taxation	32.1	1.0	9.2	42.3
<b>(Loss)/Profit for the year attributable to equity holders</b>	(151.1)	13.8	(38.6)	(175.9)

## Notes

No adjustment has been made to reflect any synergies that may arise after the transaction has completed.

No adjustment has been made to reflect the financial results of Drax Group plc or the ScottishPower Generation Group since 31 December 2017.

- (1) Drax Group plc's income statement for the year ended 31 December 2017 has been extracted without adjustment from the audited consolidated financial statements for the year ended 31 December 2017.
- (2) The ScottishPower Generation Group's income statement for the year ended 31 December 2017 has been extracted without adjustment from the historical financial information included in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) of this Circular.
- (3) The adjustments reflect:
  - The estimated transaction costs of £18 million in 'acquisition-related costs', which will be charged to the income statement as a non-recurring item.
  - Interest costs of £26.6 million on the acquisition debt raised in 'interest payable and similar charges' which is expected to be a recurring item, plus a further £3.2 million of interest costs relating to the amortisation of transaction costs relating to the bridge facility.
  - The estimated tax credit of £9.2 million arising from these costs using the standard rate of tax that applied in the year ended 31 December 2017 of 19.25 per cent.

## Part B: Accountant's Report on Pro Forma Financial Information

# Deloitte.

Deloitte LLP  
1 New Street Square  
London  
EC4A 3HQ

The Board of Directors  
on behalf of Drax Group plc  
Drax Power Station  
Selby  
North Yorkshire  
YO8 8PH

J.P. Morgan Securities plc  
25 Bank Street  
Canary Wharf  
London  
E14 5JP

5 December 2018

Dear Sirs,

### **Drax Group plc (the "Company")**

We report on the pro forma financial information (the "Pro forma financial information") set out in Part VI of the Class 1 circular dated 5 December 2018 (the "Investment Circular"), which has been prepared on the basis described in the notes, for illustrative purposes only, to provide information about how the transaction might have affected the financial information presented on the basis of the accounting policies adopted by the Company in preparing the financial statements for the period ending 31 December 2017. This report is required by the Commission Regulation (EC) No 809/2004 (the "Prospectus Directive Regulation") as applied by Listing Rule 13.3.3R and is given for the purpose of complying with that requirement and for no other purpose.

### **Responsibilities**

It is the responsibility of the directors of the Company (the "Directors") to prepare the Pro forma financial information in accordance with Annex II items 1 to 6 of the Prospectus Directive as applied by Listing Rule 13.3.3R.

It is our responsibility to form an opinion, as to the proper compilation of the Pro forma financial information and to report that opinion to you in accordance with Annex II item 7 of the Prospectus Directive Regulation as applied by Listing Rule 13.3.3R.

Save for any responsibility which we may have to those persons to whom this report is expressly addressed and which we may have as a result of the inclusion of this report in the Investment Circular, to the fullest extent permitted by law we do not assume any responsibility and will not accept any liability to any other person for any loss suffered by any such other person as a result of, arising out of, or in connection with this report or our statement, required by and given solely for the purposes of complying with Listing Rule 13.4.1R (6), consenting to its inclusion in the Investment Circular.

In providing this opinion we are not updating or refreshing any reports or opinions previously made by us on any financial information used in the compilation of the Pro forma financial information, nor do we accept responsibility for such reports or opinions beyond that owed to those to whom those reports or opinions were addressed by us at the dates of their issue.

### **Basis of Opinion**

We conducted our work in accordance with the Standards for Investment Reporting issued by the Auditing Practices Board in the United Kingdom. The work that we performed for the purpose of making this report, which involved no independent examination of any of the underlying financial information, consisted primarily of comparing the unadjusted financial information with the source documents, considering the evidence supporting the adjustments and discussing the Pro forma financial information with the Directors.



We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with reasonable assurance that the Pro forma financial information has been properly compiled on the basis stated and that such basis is consistent with the accounting policies of the Company.

Our work has not been carried out in accordance with auditing or other standards and practices generally accepted in jurisdictions outside the United Kingdom, including the United States of America, and accordingly should not be relied upon as if it had been carried out in accordance with those standards or practices.

### **Opinion**

In our opinion:

- (a) the Pro forma financial information has been properly compiled on the basis stated; and
- (b) such basis is consistent with the accounting policies of the Company.

Yours faithfully

Deloitte LLP

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## PART VII PROFIT FORECASTS

### 1. Drax 2018

In its 2017 Preliminary Results presentation, on 27 February 2018, Drax made the following statement in relation to the outlook for 2018:

*“Outlook for 2018 – continued growth in EBITDA.”*

This statement (the **“2018 Profit Forecast”**) constitutes a profit forecast for the purposes of the Listing Rules. The 2018 Profit Forecast relates to the 12 month period ending 31 December 2018, compared to the 12 month period ended 31 December 2017.

At its 2018 interim results in August 2018, and again in the announcement of the Acquisition on 16 October 2018, Drax reaffirmed this guidance noting, respectively, that *“full year expectations for 2018 are unchanged”* and *“Drax’s EBITDA expectations for the full year remain unchanged”*.

The Directors have considered and confirm that the 2018 Profit Forecast remains correct at the date of this Circular.

#### **Basis of preparation**

The 2018 Profit Forecast has been properly compiled on the basis of the assumptions stated below and on the basis of the accounting policies of the Drax Group adopted in its financial statements for the year ended 31 December 2017. Subsequent accounting policy changes include the application of IFRS15 and IFRS9 which are not expected to materially change the EBITDA results of the Drax Group. It also does not reflect the impact of IFRS16 which will apply in respect of the 2019 Annual Report and Accounts.

The 2018 Profit Forecast has been prepared with reference to:

- The unaudited actual results of Drax for the 10 months ended 31 October 2018; and
- The projected financial results of Drax for November and December 2018.

The 2018 Profit Forecast is a best estimate of the EBITDA that Drax will generate in the twelve months to 31 December 2018. Accordingly, there is a degree of uncertainty relating to the 2018 Profit Forecast and it is based on certain assumptions, which are set out below.

#### **Principal assumptions**

The 2018 Profit Forecast has been prepared on the basis of the following principal assumptions:

##### *Assumptions within management's control*

1. There is no change in the composition of the Drax Group.
2. There is no material change to the manner in which the Drax Group operates.
3. There are no material changes to the existing running costs or operating costs of the Drax Group.
4. Transaction costs and one-off costs associated with the Acquisition are not included.

##### *Assumptions outside of management's control*

1. There are no changes to recent market prices for clean spark spread, power, carbon and other commodities.
2. There are no material adverse events that have a significant impact on the performance of any of the Drax Group's assets, including more unplanned outages than would be expected in the ordinary course.
3. There are no material adverse events that have a significant impact on the Drax Group's commercial or trading activities.
4. There is no material change in the management or control of the Drax Group.

5. There is no material change to prevailing UK macroeconomic and political conditions prior to 31 December 2018.
6. No capacity payments relating to the delivery period from 1 October 2018 to 31 December 2018 are received (reflecting the suspension of payments following the Capacity Market Ruling).
7. There are no further material changes in legislation or regulatory requirements (e.g. ROCs, Capacity Market, grid charges) impacting the operations of or accounting policies applicable to the Group.

## 2. ScottishPower Generation Group 2019

On 16 October 2018, Drax announced the Acquisition. This included the following statement with respect to the ScottishPower Generation Group:

*“Expected EBITDA of £90-110 million in 2019.*

*The Portfolio is expected, based on recent power and commodity prices, to generate EBITDA in a range of £90-110 million, and gross profits of £155 million to £175 million, of which around two thirds is expected to come from non-commodity market sources, including system support services, capacity payments, Daldowie and ROCs. Pumped storage and hydro activities represent a significant proportion of the earnings associated with the portfolio.*

*For the purpose of the Profit Forecast, EBITDA is stated before any allocation of Group overheads (as these will be an allocation of the existing Drax Group cost base which is not expected to increase as a result of the acquisition of the Portfolio).”*

This statement (the **“2019 Profit Forecast”**) constitutes a profit forecast for the purposes of the Listing Rules. The 2019 Profit Forecast relates to the 12-month period ending 31 December 2019.

The Directors have considered and confirm that the 2019 Profit Forecast remains correct at the date of this Circular on the basis of the assumptions below.

The Directors note the uncertainty of the assumption concerning the receipt of contracted capacity payments due in 2019 and a sensitivity scenario in relation to this is set out below.

### **Basis of preparation**

The 2019 Profit Forecast has been properly compiled on the basis of the assumptions stated below, and on the basis of the accounting policies of the Drax Group adopted in its financial statements for the year ended 31 December 2017. Subsequent accounting policy changes include the application of IFRS15 and IFRS9 which are not initially expected to affect materially the EBITDA results of the ScottishPower Generation Group. It also does not reflect the impact of IFRS16 which will apply in respect of the 2019 Annual Report and Accounts.

The 2019 Profit Forecast has been prepared with reference to:

- unaudited 2017 financial statements based on the audited financial statements of ScottishPower Generation Limited and SMW Limited, adjusted to exclude assets and operations that do not form part of the Portfolio and restated in accordance with Drax accounting policies;
- the audited financial statements of the entities forming the Portfolio for the year ended 31 December 2017;
- the unaudited management accounts of the Portfolio for the nine months ended 30 September 2018; and
- on the basis of the projected financial performance of the Portfolio for the year ending 31 December 2019.

The 2019 Profit Forecast is a best estimate of the EBITDA that the ScottishPower Generation Group will generate for a future period of a year in respect of assets and operations that are not yet under the control of Drax. Accordingly the degree of uncertainty relating to the assumptions underpinning the 2019 Profit Forecast is inherently greater than would be the case for a profit forecast based on assets and operations under the control of Drax and/or which covered a shorter future period.

The forecast cost base reflects the expectations of the Directors of the operating regime of the Portfolio under Drax's ownership and the central support it will require.

### **Principal assumptions**

The 2019 Profit Forecast has been prepared on the basis of the following principal assumptions:

#### *Assumptions within management's control*

1. There is no change in the composition of the Portfolio.
2. There is no material change to the manner in which these assets are operated.
3. There are no material changes to the existing running costs or operating costs of the Portfolio.
4. There will be no material restrictions on running each of the assets in the Portfolio other than those that would be envisaged in the ordinary course.
5. There are no material issues with the migration of services including trading and information technology from the Seller to Drax.
6. Transaction costs and one-off costs associated with the integration are not included.

#### *Assumptions outside of management's control*

1. Completion occurs on 31 December 2018.
2. There is no material change to prevailing UK macroeconomic and political conditions prior to 31 December 2019.
3. There are no material changes in market conditions in the electricity generating market nor any changes to the UK energy supply mix.
4. All contracted capacity payments payable in respect of the Portfolio which are due in 2019 are received or accrued in 2019.
5. There are no material changes in legislation or regulatory requirements (e.g. ROCs, Capacity Market, grid charges) impacting the operations of or accounting policies applicable to the Portfolio.
6. There are no changes to recent market prices for clean spark spread, power, carbon and other commodities.
7. There is no material change from the historical 10-year average rainfall.
8. There are no material adverse events that have a significant impact on the financial performance of any of the acquired assets, including more unplanned outages than would be expected in the ordinary course.
9. Prior to Completion, the Portfolio will be operated in the ordinary course.
10. There are no material issues with the transitional services provided by the Seller to Drax pursuant to the TSA, including the migration of such services to Drax.
11. There is no material change in the management or control of the Drax Group.

### **2019 Profit Forecast sensitivity to Capacity Market Ruling**

The 2019 Profit Forecast is based on an assumption that Capacity Market payments expected to be received by the Portfolio in 2019 will be paid or accrued in full in 2019 although this assumption is subject to material uncertainty. The Directors have therefore considered a sensitivity scenario illustrating the impact if none of these payments is received or accrued in 2019.

If the Portfolio does not receive any Capacity Market payments in 2019, the 2019 Profit Forecast would be reduced by up to £47 million (from a range of £90 million to £110 million) down to a range of £43 million to £63 million before considering any mitigating factors.

Any payments pursuant to the Capacity Market Arrangement will be cash adjustments to the consideration and not included in EBITDA.

**PART VIII  
ADDITIONAL INFORMATION**

**1. Responsibility**

Drax and the Directors, whose names appear in paragraph 3 below, accept responsibility for the information contained in this Circular. To the best of the knowledge and belief of Drax and the Directors (who have taken all reasonable care to ensure that such is the case) the information contained in this Circular is in accordance with the facts and does not omit anything likely to affect the import of such information.

**2. Drax**

Drax was incorporated and registered in England and Wales as a public limited company on 13 September 2005 under the Companies Act 1985 with registered number 5562053 and the name Drax Group plc. The principal legislation under which Drax operates is the Companies Acts and the regulations made thereunder.

Drax is headquartered in the United Kingdom with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH and its telephone number is +44(0)1757 618381.

**3. The Directors and Executive Committee**

The Directors of Drax are:

<u>Name</u>	<u>Position</u>
Philip Cox CBE	Chairman
Will Gardiner	Group Chief Executive Officer
Andy Koss	Chief Executive Officer, Drax Power
David Lindsell	Senior Independent Non-Executive Director
Tim Cobbold	Independent Non-Executive Director
Tony Thorne	Independent Non-Executive Director
Nicola Hodson	Independent Non-Executive Director
David Nussbaum	Independent Non-Executive Director
Vanessa Simms	Independent Non-Executive Director

The Executive Committee of Drax comprises:

<u>Name</u>	<u>Position</u>
Will Gardiner	Group Chief Executive Officer
Andy Koss	Chief Executive Officer, Drax Power
Jonathan Kini	Chief Executive Officer, Drax Retail
Clare Harbord	Director of Corporate Affairs
Penny Small	Chief Transformation Officer

The business address of each Director and Executive Committee member is Drax's registered office.

#### 4. Directors' and Executive Committee members' interests in Ordinary Shares

##### 4.1 Holdings in Ordinary Shares

As at 3 December 2018 (being the Latest Practicable Date), the interests of each Director and Executive Committee member in the share capital of Drax are as follows:

Director	Number of Ordinary Shares held	Percentage of issued Ordinary Shares
Philip Cox CBE	60,000	0.014735
Will Gardiner	88,778	0.021803
Andy Koss	57,746	0.014182
David Lindsell	7,500	0.001842
Tim Cobbold	1,000	0.000246
Tony Thorne	7,500	0.001842
Nicola Hodson	0	0
David Nussbaum	7,500	0.001842
Vanessa Simms	0	0

Executive Committee member	Number of Ordinary Shares held	Percentage of issued Ordinary Shares
Jonathan Kini	0	0
Clare Harbord	0	0
Penny Small	0	0

##### 4.2 Other interests

As at 3 December 2018 (being the Latest Practicable Date), certain Executive Committee members have the following interests in Ordinary Shares under a number of incentive plans:

Executive Committee member	Name of share plan and award type	Grant date	Number of shares subject to award/option	Vesting/ first exercisable date
Will Gardiner	BMP Deferred	02.03.2016	5,063	02.03.2019
	BMP Matching	02.03.2016	353,504	02.03.2019
	BMP Deferred	28.03.2017	50,486	28.03.2020
	Performance Share Plan	15.03.2017	213,326	15.05.2020
	Deferred Share Plan	05.03.2018	40,327	05.03.2021
	Performance Share Plan	05.03.2018	363,725	05.03.2021
Andy Koss	BMP Matching	02.03.2016	61,999	02.03.2019
	BMP Deferred	28.03.2017	40,130	28.03.2020
	Performance Share Plan	15.05.2017	169,567	15.05.2020
	Deferred Share Plan	05.03.2018	32,055	05.03.2021
	Performance Share Plan	05.03.2018	218,063	05.03.2021
Jonathan Kini	BMP Matching	02.03.2016	87,599	02.03.2019
	Performance Share Plan	15.05.2017	70,136	15.05.2020
	Performance Share Plan	05.03.2018	98,039	05.03.2021
Clare Harbord	Performance Share Plan	15.05.2017	76,235	15.05.2020
	Performance Share Plan	05.03.2018	98,039	05.03.2021

As at 3 December 2018 (being the Latest Practicable Date), certain Executive Committee members have the following options under the Savings-Related Share Option Plan (SAYE):

Executive Committee member	Date of grant	Number of shares subject to option	Option price (£)	Maturity date
Will Gardiner	01.05.2016	14,778	203.00	01.05.2021
Andy Koss	01.05.2018	8,551	210.50	01.05.2021
Jonathan Kini	01.05.2016	8,866	203.00	01.05.2019
Clare Harbord	01.05.2018	14,251	210.50	01.05.2023

## 5. Details of the service contracts of the Directors

Details of the service contracts of the Directors are set out on page 103 of Drax's 2017 Annual Report and Accounts, save that of Vanessa Simms, who entered into a service contract for a three-year term commencing 19 June 2018, with a one-month notice period.

## 6. Major interests in shares

As at 3 December 2018 (being the Latest Practicable Date), Drax had received notification in accordance with chapter 5 of the Disclosure and Transparency Rules of the following notifiable interests in the voting rights of Ordinary Shares:

Name of Shareholder	Date notified to the stock exchange	Notified number of voting rights	Notified percentage of voting rights
Invesco Limited	19.10.2018	79,520,354	19.99%
Schroders plc	05.11.2018	55,463,866	13.96%
Artemis Investment Management LLP	20.08.2018	20,156,858	5.03%
Orbis Holdings Limited	19.10.2018	19,890,687	5.00%

## 7. Material contracts

### 7.1 Drax Group

The following contracts (not being contracts entered into in the ordinary course of business) have either: (i) been entered into by Drax or another member of the Drax Group within the period of two years immediately preceding the date of this Circular and are or may be material; or (ii) been entered into by Drax or another member of the Drax Group which contain any provisions under which any member of the Drax Group has any obligation or entitlement which is, or may be, material as at the date of this Circular:

#### (A) *Acquisition Agreement and the Transitional Services Agreement*

Details of the terms of the Acquisition Agreement, the Acquisition Agreement Amendment Deed and the Transitional Services Agreement are set out in Part IV (*Principal Terms of the Acquisition*).

#### (B) *Acquisition Facility Agreement*

Drax Corporate entered into an acquisition bridge facility agreement on 16 October 2018 between Drax Corporate as borrower, Drax Group Holdings as original guarantor, Barclays Bank PLC, Bank of America Merrill Lynch International Limited and J.P. Morgan Securities plc as mandated lead arrangers, Barclays Bank PLC as facility agent, and Barclays Bank PLC, Bank of America Merrill Lynch International Limited and JPMorgan Chase Bank, N.A., London Branch as original lenders.

Under the Acquisition Facility Agreement the lenders will make available the Acquisition Facility, a £725 million committed acquisition facility, including without limitation, a certain funds facility for the purposes of the Acquisition.

#### Borrower and guarantors

Drax Corporate is the borrower under the Acquisition Facility Agreement. The Acquisition Facility will be guaranteed on a joint and several basis by the Guarantors, which are Drax Group Holdings and certain subsidiaries of Drax Group Holdings.

#### Security

The finance parties under the Acquisition Facility Agreement will (subject to certain agreed security principles) have the benefit of first ranking security over: (i) the issued share capital of Drax Group Holdings; (ii) certain receivables owed to Drax by Drax Group Holdings; (iii) the issued share capital of Drax Corporate and each Guarantor and (iv) substantially all of the assets of Drax Group Holdings, Drax Corporate and each Guarantor (other than any real property located in the United States) (together, the “**Common Security**”). The Acquisition Facility may be secured by further security interests from time to time subject to certain agreed security principles.

The Acquisition Facility will be subject to the provisions of the Intercreditor Agreement. Under the terms of the Intercreditor Agreement, in the event of an enforcement of the Common Security, the lenders under the Acquisition Facility Agreement will receive proceeds from the enforcement of the Common Security or from certain distressed disposals of the Common Security pari passu with the holders of the 2022 Notes and the 2025 Notes and only after certain other creditors, including the lenders under the Senior Facilities Agreement and counterparties to certain hedging obligations (including the obligations under the Secured Trading Line) have been repaid in full.

#### Purpose

Each loan under the Acquisition Facility may be used for (i) the Acquisition and related costs or (ii) general corporate purposes of the Restricted Group up to an aggregate limit of £75 million.

#### Availability and maturity

The Acquisition Facility is available to be drawn for the purposes of the Acquisition and related costs up until the earliest of the first utilisation date of the Acquisition Facility, the Long Stop Date and the date falling eight months after 13 October 2018.

The Acquisition Facility is available to be drawn for general corporate purposes up until the earlier of the date falling one month prior to the maturity date of the Acquisition Facility and the first date on which any member of the Restricted Group receives the proceeds of any equity raise, debt capital markets issuance or loan financing which are required to be applied to prepay the Acquisition Facility, as described below.

The Acquisition Facility will mature on the date falling twelve months from the date of the first utilisation of the Acquisition Facility, with an option for Drax Corporate to extend for a further seven months.

#### Prepayment / cancellation

The Acquisition Facility Agreement contains provisions for voluntary prepayment, mandatory prepayment (on the occurrence of certain events including change of control, illegality and sale of all or substantially all of the assets of the Restricted Group) and cancellation. The Acquisition Facility Agreement provides for mandatory prepayment of net proceeds arising from any equity raise, debt capital markets issuance or loan financing by any member of the Restricted Group (except as specifically provided for) and makes provision for mandatory prepayment for disposals (over specified thresholds and subject to certain conditions) and in respect of recovery claims made against the Seller.



The Acquisition Facility Agreement also contains customary provisions for the prepayment and cancellation of a particular lender's commitments in the case of a defaulting lender, additional payments being charged for tax reasons or increased costs.

#### Interest

Interest is payable under the Acquisition Facility at a rate of LIBOR plus the applicable margin. The margin will step up after three, six, twelve and seventeen months following the first date of utilisation of the Acquisition Facility, and ranges from a minimum of 0.75 per cent. per annum to a possible maximum of 2.75 per cent. per annum.

#### Financial covenants

The Acquisition Facility Agreement does not contain any financial covenants.

#### Representations, covenants and events of default

The Acquisition Facility Agreement contains negative covenants, affirmative covenants, representations and events of default that are substantially similar to those in the Senior Facilities Agreement, as described below, save that (i) there are no such representations, covenants or events of default relating to the Secured Trading Line and (ii) there is no negative covenant in respect of disposals of assets to non-obligor subsidiaries and no affirmative covenant in relation to guarantor coverage, but instead there is an affirmative covenant requiring any guarantors under the Senior Facilities Agreement, the 2022 Notes Indenture or the 2025 Notes Indenture to guarantee the Acquisition Facility, subject to certain exceptions.

#### Governing law

The Acquisition Facility Agreement is governed by and construed and enforced in accordance with English law, although the incurrence covenants contained therein, which largely replicate the relevant covenants from the 2022 Notes, are interpreted in accordance with the laws of the State of New York.

### (C) *Senior Facilities Agreement*

Drax Power, as borrower, entered into a revolving credit facility agreement on 20 December 2012 between, among others, Drax Power, Barclays Bank PLC as facility agent and Drax Corporate, which was amended and restated pursuant to an amendment and restatement agreement on 21 April 2017, with effect from 5 May 2017. The Senior Facilities Agreement comprises a £315 million committed multicurrency working capital and ancillary facility, including, without limitation, a letter of credit facility (the "**Revolving Facility**") and a £35 million term facility (the "**Term Loan**") (the Revolving Facility and the Term Loan together, the "**Senior Facilities**"). The Revolving Facility can be drawn in pound sterling, euro or US dollars. The Term Loan was fully drawn on 5 May 2017.

#### Borrowers and guarantors

The original borrower under the Senior Facilities Agreement is Drax Corporate. The Senior Facilities Agreement provides for the flexibility of acceding (and subsequently resigning) subsidiaries of Drax Group Holdings incorporated in the UK or in the US (subject to certain customary conditions) as additional borrowers. The Senior Facilities are guaranteed on a joint and several basis by Drax Group Holdings and each of the Guarantors.

#### Security

The finance parties under the Senior Facilities Agreement have the benefit of the Common Security. The Senior Facilities may be secured by further security interests from time to time subject to certain agreed security principles set out in the Senior Facilities Agreement.

The Senior Facilities Agreement is subject to the provisions of the Intercreditor Agreement. Under the terms of the Intercreditor Agreement, the proceeds from any distressed disposal and from any enforcement of the Common Security will be applied to repayment of the Senior Facilities and certain hedging obligations (including obligations under the Secured Trading Line) in priority to repayment of the 2022 Notes, the 2025 Notes and the Acquisition Facility.

#### Purpose

Each loan under the Revolving Facility may be used: (i) to provide cash collateral in favour of certain permitted counterparties; (ii) to provide cash cover in favour of an issuing bank of a letter of credit or in respect of an ancillary facility under the Senior Facilities Agreement; and (iii) for the other general corporate purposes of the Restricted Group, including, but not limited to, financing working capital requirements. There is a separate sub-limit of £200 million on cash drawings for general corporate purposes under limb (iii) above.

#### Availability and maturity

The Revolving Facility is available to be drawn until one month prior to the final maturity date and letters of credit may be issued up until the final maturity date (in each case, as such may be extended). The Revolving Facility has an initial maturity date of 30 April 2021, with an option to extend to 30 April 2022. The Term Loan has a maturity date of 31 March 2022.

The Revolving Facility may be utilised by way of letter of credit, reducing the amount available for cash drawings under the Revolving Facility by an amount equivalent to the letters of credit issued.

#### Prepayment / cancellation

The Senior Facilities Agreement contains customary provisions for the prepayment and cancellation of a particular lender's commitments in the case of a defaulting lender, additional payments being charged for tax reasons or increased costs.

Subject to certain conditions, the borrowers under the Revolving Facility may voluntarily prepay their utilisations or permanently cancel all or part of the available commitments under the Revolving Facility. Amounts voluntarily prepaid may be re-borrowed during the availability period applicable to the Revolving Facility. Subject to certain conditions, the borrower of the Term Loan may voluntarily prepay all or part of the Term Loan at an amount equal to the principal amount so prepaid multiplied by the index ratio as at the relevant prepayment date, plus a make-whole amount (as described below).

Subject to certain thresholds and other qualifications, there are mandatory prepayments required to be made in respect of the Senior Facilities upon the occurrence of certain events such as change of control, illegality and sale of all or substantially all of the assets of the Restricted Group. The Senior Facilities Agreement also contains provisions for mandatory prepayment on certain purchases or redemptions of the 2022 Notes. There is also a mandatory prepayment required to be made in respect of the Term Loan in the event that the applicable index ceases to be published and no appropriate successor index can be determined. The applicable make-whole amount, as described further below, is payable in respect of prepayments under the Term Loan.

The applicable make-whole amount in respect of prepayments under the Term Loan is calculated by reference to the excess, if any, of the discounted value of the remaining scheduled payments of principal and interest under the Term Loan with respect to the principal amount prepaid, over the amount of such principal prepaid. The applicable discount factor is calculated by reference to the applicable percentage (which is determined by reference to the nature of the relevant prepayment) plus the yield to maturity of the specified reference gilt.

#### Interest

Interest is payable under the Revolving Facility at a rate of LIBOR or, in the case of loans in euro, EURIBOR (in each case subject to a zero floor) plus the applicable margin. Save for in

circumstances where an event of default has occurred and is continuing or the borrower has failed to notify the facility agent of a change in rating, the applicable margin is determined by reference to a ratings matrix, ranging from a maximum of 2.75 per cent. where the rating of the debt incurred under the Revolving Facility is BB-/Ba3 or lower to a minimum of 1.25 per cent. where such rating is BBB/Baa2 or higher.

Interest is payable under the Term Loan at a rate calculated by multiplying a fixed rate of 4.158 per cent. per annum by the index ratio applicable to the relevant interest payment date multiplied by the outstanding principal amount of the Term Loan. The relevant index for calculation of the index ratio is the Non-revised Retail Price Index All Items in the United Kingdom as published by the Office for National Statistics.

#### Financial covenants

The Senior Facilities Agreement contains a financial covenant requiring the Restricted Group's consolidated EBITDA for the prior twelve-month period to be no less than £170 million as at any applicable semi-annual testing date. This covenant will be tested only where either: (i) drawings of cash within the £200 million sub-limit on cash drawings for general corporate purposes described above are 25 per cent. or more of the total commitments as at the relevant semi-annual testing date; or (ii) any Term Loan is outstanding.

#### Representations, covenants and events of default

The Senior Facilities Agreement contains certain negative covenants that are substantially similar to those in the 2022 Notes Indenture governing the 2022 Notes, as described below. The Senior Facilities Agreement also contains customary negative covenants, subject to certain agreed exceptions, including, but not limited to, (i) restrictions on change of business; (ii) centre of main interests; (iii) share capital; (iv) purchase or redemption of the 2022 Notes; (v) activities of Drax Group Holdings; (vi) incurrence of certain indebtedness by non-obligor subsidiaries; (vii) certain disposals of assets to non-obligor subsidiaries; (viii) changes to Drax's year end; and (ix) parameters of the Secured Trade Line.

The Senior Facilities Agreement also requires each obligor to observe certain affirmative covenants subject to materiality and other customary and agreed exceptions. These affirmative covenants include, but are not limited to, covenants related to: (i) compliance with relevant laws rules and regulations (including environmental, sanctions and anti-corruption); (ii) payment of taxes; (iii) the delivery of certain financial statements; (iv) information reporting obligations in respect of the Secured Trading Line; (v) rating; (vi) notice of default and material litigation; (vii) right to request information relating to the Drax Group's financial condition; (viii) insurance; (ix) maintenance of assets; and (x) compliance with and maintenance of material authorisations. There is also an affirmative covenant in relation to guarantor coverage (by reference to 85 per cent. of the Restricted Group's consolidated EBITDA and consolidated total assets), subject to certain exceptions. The Senior Facilities Agreement also contains representations that are customary for debt facilities of this nature.

The Senior Facilities Agreement contains customary events of default (subject in certain cases to agreed thresholds, grace periods and qualifications), including non-payment, breach of other obligations, misrepresentation, cross-default, insolvency, insolvency proceedings, creditors' process, cessation of business, effectiveness of finance documents, ownership of obligors and proceedings. In addition to these customary events of default, the Senior Facilities Agreement contains events of default reflective of the nature of the Drax Group's business, relating to the generation licence granted to Drax Power pursuant to the Electricity Act 1989, nationalisation, and the Secured Trading Line. At any time after the occurrence of an event of default, the facility agent may, and on the instruction of majority lenders must, cancel all or any part of the total commitments and/or declare that amounts outstanding are immediately due and payable and/or payable on demand. In addition, after the occurrence of an event of default following a breach of the financial covenant described above, the lenders under the Term Loan and the majority lenders under the Revolving Facility each have a separate right (in respect of the Term Loan and the Revolving Facility, respectively) to cancel all or any part of the commitments and/or declare that amounts outstanding are immediately due and payable and/or payable on demand.

### Governing law

The Senior Facilities Agreement is governed by and construed and enforced in accordance with English law, although the incurrence covenants contained therein, which largely replicate the relevant covenants from the 2022 Notes, are interpreted in accordance with the laws of the State of New York.

#### (D) *2022 Notes Indenture*

On 5 May 2017, Drax Finco issued £350 million aggregate principal amount of 4.250 per cent. Senior Secured Notes due 2022 under an indenture dated as of 5 May 2017, as amended and restated from time to time.

The 2022 Notes will mature on 1 May 2022. The 2022 Notes were issued in minimum denominations of £100,000 and in integral multiples of £1,000 in excess thereof. The 2022 Notes are listed on the Official List of the Luxembourg Stock Exchange and admitted to trading on the Euro MTF Market thereof.

### Guarantees and security

The 2022 Notes are guaranteed on a joint and several basis by Drax Group Holdings, Drax Corporate and each of the Guarantors (other than Drax Finco).

The 2022 Notes and the guarantees thereof are secured by the Common Security. The 2022 Notes may be secured by further security interests from time to time subject to certain agreed security principles set out in the Senior Facilities Agreement.

The 2022 Notes are subject to the provisions of the Intercreditor Agreement. Under the terms of the Intercreditor Agreement, in the event of an enforcement of the Common Security, the holders of the 2022 Notes will receive proceeds from the enforcement of the Common Security or from certain distressed disposals of the Common Security pari passu with the holders of the 2025 Notes and the lenders under the Acquisition Facility Agreement and only after certain other creditors, including the lenders under the Senior Facilities Agreement and counterparties to certain hedging obligations (including the obligations under the Secured Trading Line) have been repaid in full.

### Prepayments and redemption

At any time prior to 1 May 2019, Drax Finco may on any one or more occasions redeem up to 40 per cent. of the original principal amount of the 2022 Notes, subject to the terms of, and at the redemption prices specified in, the 2022 Notes Indenture, plus accrued and unpaid interest and additional tax amounts to the redemption date, with the proceeds of an equity offering provided that: (i) at least 60 per cent. of the original principal amount of the 2022 Notes issued under the 2022 Notes Indenture remains outstanding after each such redemption, and (ii) the redemption occurs within 180 days after the closing of such equity offering.

At any time prior to 1 May 2019, Drax Finco may redeem all or, from time to time, part of the 2022 Notes, subject to the terms of the 2022 Notes Indenture, and at a redemption price equal to 100 per cent. of the principal amount of the 2022 Notes, plus the applicable premium plus accrued and unpaid interest and additional tax amounts to the redemption date.

On and after 1 May 2019, Drax Finco may redeem all or, from time to time, part of the 2022 Notes, subject to the terms of, and at the redemption prices specified in, the 2022 Notes Indenture, plus accrued and unpaid interest and additional tax amounts to the redemption date.

In connection with any tender offer for, or other offer to purchase, all of the 2022 Notes, in the event that holders of not less than 90 per cent. of the aggregate principal amount of the outstanding 2022 Notes validly tender and do not validly withdraw such 2022 Notes in such tender offer or offer to purchase and Drax Finco or a third party making such tender offer or offer to purchase all the 2022 Notes held by such holders, within 60 days of such purchase, Drax Finco will have the right, upon not less than 10 and no more than 60 days' prior notice,

to redeem all (but not less than all) the 2022 Notes of the same series that remain outstanding following such purchase at a redemption price equal to the highest price (excluding any early tender premium or similar payment) paid to each other holder in such tender offer or offer to purchase, plus, to the extent not included in the tender offer or offer to purchase payment, accrued and unpaid interest to the date of such redemption.

Upon the occurrence of certain events constituting a change of control, Drax Finco may be required to make an offer to repurchase the 2022 Notes at a redemption price equal to 101 per cent. of the principal amount of the 2022 Notes repurchased, plus accrued and unpaid interest and additional tax amounts to the date of purchase.

Drax Finco may redeem the 2022 Notes in whole, but not in part, at any time in certain circumstances if Drax Finco determines in good faith that, as a result of any change in tax law in any applicable tax jurisdiction, Drax Finco would become obligated to pay additional amounts on payments on the 2022 Notes.

Subject to the provisions of the Intercreditor Agreement, Drax Finco may repurchase 2022 Notes at any time and from time to time in the open market or otherwise.

#### Interest

Interest on the 2022 Notes accrues at a rate of 4.250 per cent. per annum and is payable in cash semi-annually in arrear on 1 May and 1 November of each year.

#### Covenants and events of default

The 2022 Notes Indenture contains a number of negative covenants that, among other things, restrict, subject to certain exceptions, the ability of any member of the Restricted Group to: (i) incur or guarantee additional indebtedness, (ii) make investments or other restricted payments, (iii) pay dividends or make other distributions or purchase or redeem stock, (iv) enter into agreements that restrict the Restricted Group's ability to pay dividends, (v) transfer or sell assets, (vi) engage in transactions with affiliates, (vii) create or permit to exist liens on assets to secure indebtedness, and (viii) impair or consolidate with or into another company. Each of these covenants is subject to significant exceptions and qualifications.

In addition, the 2022 Notes Indenture imposes certain requirements as to future subsidiary guarantors, including an affirmative covenant in relation to guarantor coverage (by reference to 80 per cent. of the Restricted Group's consolidated EBITDA and consolidated total assets), subject to certain exceptions, and contains certain customary events of default.

#### Governing law

The 2022 Notes Indenture and the 2022 Notes, and the rights and duties of the parties thereunder, are governed by and construed in accordance with the laws of the State of New York.

#### (E) *2025 Notes Indenture*

On 26 April 2018, Drax Finco issued US\$300 million aggregate principal amount of 6.625 per cent. Senior Secured Notes due 2025 under an indenture dated as of 26 April 2018, as amended and restated from time to time.

The 2025 Notes will mature on 1 November 2025. The 2025 Notes were issued in minimum denominations of US\$200,000 and in integral multiples of US\$1,000 in excess thereof. The 2025 Notes are listed on the Official List of the Luxembourg Stock Exchange and admitted to trading on the Euro MTF Market thereof.

#### Guarantees and security

The 2025 Notes are guaranteed on a joint and several basis by Drax Group Holdings, Drax Corporate and each of the Guarantors (other than Drax Finco).

The 2025 Notes and the guarantees thereof are secured by the Common Security. The 2025 Notes may be secured by further security interests from time to time subject to certain agreed security principles set out in the Senior Facilities Agreement.

The 2025 Notes are subject to the provisions of the Intercreditor Agreement. Under the terms of the Intercreditor Agreement, in the event of an enforcement of the Common Security, the holders of the 2025 Notes will receive proceeds from the enforcement of the Common Security or from certain distressed disposals of the Common Security pari passu with the holders of the 2025 Notes and the lenders under the Acquisition Facility Agreement and only after certain other creditors, including the lenders under the Senior Facilities Agreement and counterparties to certain hedging obligations (including the obligations under the Secured Trading Line) have been repaid in full.

#### Prepayments and redemption

At any time prior to 1 May 2021, Drax Finco may on any one or more occasions redeem up to 40 per cent. of the original principal amount of the 2025 Notes, subject to the terms of, and at the redemption prices specified in, the 2025 Notes Indenture, plus accrued and unpaid interest and additional tax amounts to the redemption date, with the proceeds of an equity offering provided that: (i) at least 50 per cent. of the original principal amount of the 2025 Notes issued under the 2025 Notes Indenture remains outstanding after each such redemption, and (ii) the redemption occurs within 180 days after the closing of such equity offering.

At any time prior to 1 May 2021, Drax Finco may redeem all or, from time to time, part of the 2025 Notes, subject to the terms of the 2025 Notes Indenture, and at a redemption price equal to 100 per cent. of the principal amount of the 2025 Notes, plus the applicable premium plus accrued and unpaid interest and additional tax amounts to the redemption date.

On and after 1 May 2021, Drax Finco may redeem all or, from time to time, part of the 2025 Notes, subject to the terms of, and at the redemption prices specified in, the 2025 Notes Indenture, plus accrued and unpaid interest and additional tax amounts to the redemption date.

In connection with any tender offer for, or other offer to purchase, all of the 2025 Notes, in the event that holders of not less than 90 per cent. of the aggregate principal amount of the outstanding 2025 Notes validly tender and do not validly withdraw such 2025 Notes in such tender offer or offer to purchase and Drax Finco or a third party making such tender offer or offer to purchase all the 2025 Notes held by such holders, within 60 days of such purchase, Drax Finco will have the right, upon not less than 10 and no more than 60 days' prior notice, to redeem all (but not less than all) the 2025 Notes of the same series that remain outstanding following such purchase at a redemption price equal to the highest price (excluding any early tender premium or similar payment) paid to each other holder in such tender offer or offer to purchase, plus, to the extent not included in the tender offer or offer to purchase payment, accrued and unpaid interest to the date of such redemption.

Upon the occurrence of certain events constituting a change of control, Drax Finco may be required to make an offer to repurchase the 2025 Notes at a redemption price equal to 101 per cent. of the principal amount of the 2025 Notes repurchased, plus accrued and unpaid interest and additional tax amounts to the date of purchase.

Drax Finco may redeem the 2025 Notes in whole, but not in part, at any time in certain circumstances if Drax Finco determines in good faith that, as a result of any change in tax law in any applicable tax jurisdiction, Drax Finco would become obligated to pay additional amounts on payments on the 2025 Notes.

Subject to the provisions of the Intercreditor Agreement, Drax Finco may repurchase 2025 Notes at any time and from time to time in the open market or otherwise.

#### Interest

Interest on the 2025 Notes accrues at a rate of 6.625 per cent. per annum and is payable in cash semi-annually in arrear on 1 May and 1 November of each year.

### Covenants and events of default

The 2025 Notes Indenture contains a number of negative covenants that, among other things, restrict, subject to certain exceptions, the ability of any member of the Restricted Group to: (i) incur or guarantee additional indebtedness; (ii) make investments or other restricted payments; (iii) pay dividends or make other distributions or purchase or redeem stock; (iv) enter into agreements that restrict the Restricted Group's ability to pay dividends; (v) transfer or sell assets; (vi) engage in transactions with affiliates; (vii) create or permit to exist liens on assets to secure indebtedness; and (viii) impair or consolidate with or into another company. Each of these covenants is subject to significant exceptions and qualifications. In addition, the 2025 Notes Indenture contains certain customary events of default.

### Governing law

The 2025 Notes Indenture and the 2025 Notes, and the rights and duties of the parties thereunder, are governed by and construed in accordance with the laws of the State of New York.

#### (F) *Investment contract relating to the Drax 3rd Conversion Unit (Unit 1)*

On 9 May 2014, Drax Power (a member of the Drax Group) entered into the Investment Contract, a contract relating to Unit 1, its third coal-to-biomass conversion unit, with the Secretary of State for Energy and Climate Change. Such investment contracts were introduced by the UK Government to support the development of low-carbon electricity and to encourage the renewables sector.

The Investment Contract works by stabilising revenues attributed to Drax Power's Unit 1 at a fixed price level known as the "strike price". Unit 1 will receive revenue from selling electricity into the market as usual. However, when the market reference price (as specified in the Investment Contract) is below the strike price, Drax Power will receive a payment to cover the difference. Conversely, if the market reference price is above the strike price, Drax Power will be required to make a payment for the difference. The effect of the Investment Contract is therefore to remove the uncertainty of Drax Power's revenue stream in relation to Unit 1 until 31 March 2027 when the term of the Investment Contract expires.

The Investment Contract is subject to the Investment Contract Standard Terms and Conditions dated 9 May 2014 which require Drax Power to meet certain requirements and milestones and provide for early termination of the Investment Contract in the event that Drax Power is unable to meet certain of its obligations under the Investment Contract.

#### (G) *Trading*

Drax Power has entered into ISDA agreements (the "**STL Master Agreements**") with a number of financial institutions (the "**STL Counterparties**"), under which Drax Power can trade UK power, dark green spreads and gas on a senior secured basis without the requirement for Drax Power to post collateral. This arrangement is known as the Secured Trading Line. Certain minimum rating requirements are imposed on the STL Counterparties under the ISDA agreements, and STL Counterparties that fail to meet such requirements shall post collateral to Drax Power to the extent of any exposure Drax Power faces on transactions with that STL Counterparty.

The tradable volumes and maximum exposure permitted under the Secured Trading Line are set on a seasonal basis, based upon parameters set out in the Senior Facilities Agreement. Trading is limited at any time to five consecutive six-monthly seasons, commencing with winter 2017/18 and subject to extension by Drax Power at its discretion at the end of each season, within the parameters of the Senior Facilities Agreement. Under the terms of the Senior Facilities Agreement, the potential future exposure under the Secured Trading Line for each combination of tradable products must be less than £200 million as determined on a seasonal basis, with the maximum seasonal trading volume being up to 600MW (or equivalent). The £200 million cap, for each combination of tradable products, remains in effect to control the voting rights of the STL Counterparties only, and does not limit their

super senior secured claims under the Secured Trading Line, which will be determined in accordance with the terms of the underlying Secured Trading Line documents and which are uncapped.

Potential future exposure under the Secured Trading Line is calculated on the basis of the net aggregate mark-to-market exposure of all transactions entered into under the Secured Trading Line and the net aggregate forecast mark-to-market exposure as if the maximum seasonal trading volume were to be traded for each of the relevant seasons. However, the actual day-to-day level of exposure will fluctuate and may cross the £200 million threshold should the forecast exposure fall short of actual levels.

The STL Counterparties' right to terminate all or any part of a transaction entered into with Drax Power under the relevant STL Master Agreement is prescribed by the Intercreditor Agreement and the Senior Facilities Agreement. These extend beyond the usual termination rights under an ISDA agreement, for instance the right to terminate if Drax Power enters into a transaction under the STL Master Agreement which results in the maximum seasonal trading volume threshold being exceeded.

The STL Counterparties benefit from the Common Security, as described above.

In addition, the Drax Group has outstanding currency rate hedging arrangements and has the ability to enter into additional currency, interest rate and inflation rate hedging arrangements on a secured basis, with the counterparties to such hedging arrangements also benefiting from the Common Security as referred to above.

These arrangements are in addition to any commodities and/or currency and interest rate trading that the Drax Group undertakes on an unsecured and/or title transfer collateral basis.

(H) *Haven Power MRTSA*

Haven Power Limited ("**Haven Power**") has entered into a master receivables and transfer and servicing agreement ("**Haven Power MRTSA**"), under which Haven Power as seller and servicer sells trade receivables to Ester Finance Titrisation as purchaser, with Crédit Agricole Corporate and Investment Bank as the arranger and calculation agent and Eurotitrisation as the programme agent.

Drax Group Holdings guarantees Haven Power's obligations under the Haven Power MRTSA.

(I) *OCGT developments*

On 5 December 2016, Drax Developments entered into an agreement with Watt Power Limited, a developer of OCGT assets, to acquire four companies each holding a 299MW OCGT development project. OCGTs can be used by Drax to provide flexible support to the electricity system to make up any shortfall in generation.

Two of these projects are in an advanced stage of development and participated in the 2016 and February 2018 T-4 Capacity Market auctions, although exited above the clearing price on both occasions. Both projects have prequalified for the February 2019 T-4 Capacity Market auction.

The other two projects are currently in the planning and consenting phase of development and are targeting participation in future T-4 Capacity Market auctions.

The initial purchase price under the agreement for all four companies was £18.5 million, with the total consideration payable dependent on the clearing price in future Capacity Market auctions.

(J) *Opus Acquisition Agreement*

Details of the terms of the acquisition agreement relating to the acquisition by Drax of Opus Energy Group Limited are set out in Part IV (*Principal Terms of the Acquisition*) of the Opus Circular, which Part is incorporated by reference into this Circular.



## 7.2 ScottishPower Generation Group

The following contracts (not being contracts entered into in the ordinary course of business) have either: (i) been entered into by SPGEN or another member of the ScottishPower Generation Group within the period of two years immediately preceding the date of this Circular and are or may be material; or (ii) been entered into by SPGEN or another member of the ScottishPower Generation Group which contain any provisions under which any member of the ScottishPower Generation Group has any obligation or entitlement which is, or may be, material as at the date of this Circular:

### (A) *SPUK plc Guarantee*

On 4 November 1997, Scottish Power UK plc entered into a trust deed with The Law Debenture Trust Corporation plc in connection with a debt issuance programme under which Scottish Power UK plc would issue certain debt securities to various investors (the “Notes”). A supplemental trust deed (the “**SPUK plc Guarantee**”) was subsequently entered into by Scottish Power UK plc, as issuer of the Notes (the “**Issuer**”), The Law Debenture Trust Corporation plc, as trustee on behalf of the holders of the Notes (the “**Trustee**”), and SP Distribution Limited, SP Transmission Limited and SPGEN (each a “**SPUK plc Guarantor**” and together the “**SPUK plc Guarantors**”). Pursuant to the SPUK plc Guarantee, SPGEN together with the other SPUK plc Guarantors, unconditionally and irrevocably guaranteed, on a joint and several basis, the payment obligations of the Issuer under the Notes. As at the date of signing the Acquisition Agreement, the total outstanding debt owed by Scottish Power UK plc was approximately £1.1 billion.

Under the terms of the Acquisition Agreement, the Seller is under an obligation, at its own cost, to secure the release or discharge of SPGEN from the SPUK plc Guarantee with effect on or prior to Completion and to provide written evidence of the same to Drax. Prior to such release or discharge, the Seller has also undertaken to indemnify Drax in relation to any liabilities connected with or arising out of the SPUK plc Guarantee.

### (B) *Daldowie & Shieldhall PFI Agreement*

On 6 December 1999, the West of Scotland Water Authority (succeeded by Scottish Water) and SMW entered into an agreement pursuant to which SMW agreed to arrange for the design, construction, financing and ongoing operation of the sludge transfer and treatment facilities at Daldowie and Shieldhall (the “**Daldowie & Shieldhall PFI Agreement**”). Construction of the facilities was completed in November 2002.

#### Term & services

The current term of the Daldowie & Shieldhall PFI Agreement expires in April 2026. During the remainder of the current term, SMW is required to perform certain services in relation to the facilities, including sludge receipt, sludge treatment, sludge disposal, waste disposal and the operation and maintenance of the facilities.

#### Negative covenants

SMW is subject to a number of negative covenants which, subject to certain exceptions, include a prohibition on SMW, without the prior consent of Scottish Water, incurring any indebtedness or creating any security interest over any part of its assets or business undertaking.

#### Termination

Scottish Water may terminate the Daldowie & Shieldhall PFI Agreement in the event of certain defaults by SMW specified under the agreement (including, for example, insolvency or material unremedied breach of the agreement). Scottish Water may also terminate the Daldowie & Shieldhall PFI Agreement at any time by providing not less than six months’ notice to SMW. In the event of such termination on notice, Scottish Water is obligated to pay SMW compensation in accordance with calculation mechanics provided under the terms of the Daldowie & Shieldhall PFI Agreement.

SMW may terminate the Daldowie & Shieldhall PFI Agreement in the event of certain defaults by Scottish Water specified under the agreement (including, for example, insolvency or material unremedied breach of the agreement).

#### Handover

Upon the expiry of the Daldowie & Shieldhall PFI Agreement (whether at the end of its term or due to an earlier termination by either party, including Scottish Water's right to terminate on six months' notice), Scottish Water may require SMW to assign its interests in the facilities at Daldowie and/or Shieldhall to Scottish Water, on such terms as Scottish Water reasonably requires. If Scottish Water makes this election, Scottish Water is obligated to pay SMW compensation in accordance with calculation mechanics provided under the terms of the Daldowie & Shieldhall PFI Agreement. Additionally, if Scottish Water makes such an election, SMW will also be required to sell, at market value, all equipment and materials owned by SMW which are required in the performance of SMW's services at the relevant facilities.

#### Step-in rights of Scottish Water

Scottish Water has step-in rights under the Daldowie & Shieldhall PFI Agreement which may be triggered in certain circumstances, including on the occurrence of a breach by SMW of an obligation under the Daldowie & Shieldhall PFI Agreement which does or is likely to: (i) create an immediate and serious threat to health and safety, the environment or a serious nuisance; (ii) result in a material interruption to the provision of a material part of the services provided under the agreement; or (iii) cause Scottish Water to breach its statutory obligations.

#### Super Profits

If, on the expiry of the term or the termination of the Daldowie & Shieldhall PFI Agreement or the transfer of the share capital of SMW, the post-tax cash flows earned by SMW during the term of the Daldowie & Shieldhall PFI Agreement would exceed certain specified limits, SMW will be obligated to pay Scottish Water 50 per cent. of the amount by which the total amount of those cash flows exceeds the specified limits (such excess constituting "**Super Profits**"). SMW is required during the term of the Daldowie & Shieldhall PFI Agreement to monitor on an annual basis the extent to which any Super Profits may become payable. Not less than 24 months prior to the expected expiry of the term of the agreement, SMW is obliged to notify Scottish Water of its anticipated liability in respect of Super Profits and to provide credit support in respect of such payment obligations in the form of a parent company guarantee, a bank bond or an escrow account.

## **8. Litigation**

### **8.1 Drax**

There are no, nor have there been any, governmental, legal or arbitration proceedings (nor is Drax aware of any such proceedings being pending or threatened by or against any member of the Drax Group) which may have, or during the last twelve months prior to the date of this Circular have had, a significant effect on the financial position or profitability of the Drax Group.

### **8.2 ScottishPower Generation Group**

Except as provided below, there are no, nor have there been any, governmental, legal or arbitration proceedings (nor are the Directors or the Company aware of any such proceedings being pending or threatened by or against any member of the ScottishPower Generation Group) which may have, or during the last 12 months prior to the date of this Circular have had, a significant effect on the financial position or profitability of the ScottishPower Generation Group.

On 15 November 2018, the General Court of the European Union issued the Capacity Market Ruling. The Capacity Market Ruling imposed a "standstill period" while the European Commission completes a further State aid investigation into the Capacity Market. Payments to generators scheduled under existing capacity agreements and the holding of future capacity auctions have been suspended.

Contracted capacity payments make up a significant proportion of the earnings of the ScottishPower Generation Group, with many of the assets in the Portfolio benefitting from the right to receive such payments under existing capacity agreements. For the period from 1 January 2019 to 30 September 2022, the Cruachan pumped storage hydro asset has contracted capacity payments of £29 million, the Galloway run-of-river hydro assets have contracted capacity payments of £5 million, and the Damhead Creek, Rye House, Shoreham and Blackburn CCGT assets have contracted capacity payments of £122 million in aggregate.

The Directors note the UK Government's statement in response to the Capacity Market Ruling that it is working closely with the European Commission to aid their investigation and to seek a timely State aid re-approval decision for the Capacity Market. The UK Government has also confirmed that the Capacity Market Ruling does not change its belief that Capacity Market auctions are the most appropriate way to deliver secure electricity supplies at the lowest cost. The UK Government has also noted that the Capacity Market Ruling was decided on procedural grounds and did not constitute a direct challenge to the design of the Capacity Market mechanism itself.<sup>4</sup>

National Grid has confirmed that the T-4 and T-1 auctions for the years 2022/23 and 2019/20, which were scheduled for February 2019 and January 2019 respectively, have been postponed in light of the "standstill period". National Grid has advised capacity agreement holders that the UK Government is doing everything in its power to re-obtain State aid approval as soon as possible, and that the UK Government intends to seek a separate State aid approval to run a one-off "replacement" T-1 Auction in 2019. The Directors note that National Grid has also confirmed that it intends to run the postponed T-4 for 2022/23 as a T-3 Auction in the 2019 auction round, subject to the European Commission completing its formal investigation and providing State aid approval for the Capacity Market.<sup>5</sup>

The UK Government has confirmed it is working to reinstate the full Capacity Market regime and is in discussions with the European Commission regarding the swiftest means of doing so.

Based on the information available to them and legal advice they have received, the Directors believe the most likely outcome is that the European Commission will re-approve the existing Capacity Market in its current form or a broadly similar form. The Directors recognise there is some uncertainty whether, if the Capacity Market is reinstated in its current form, the contracted capacity payments for the Capacity Market year 2018/2019 which are currently suspended will be paid by the UK Government. To mitigate the risk that these payments are not received for the 2018/2019 Capacity Market year, Drax has agreed with Iberdrola S.A. certain amendments to the Acquisition Agreement signed on 16 October 2018 pursuant to the Acquisition Agreement Amendment Deed. The Directors believe that the arrangements provided in the amended Acquisition Agreement mitigate in economic terms the majority of the risk that those suspended capacity payments will not be paid.

The Directors believe that the most likely outcome after 2019 is that existing capacity agreements for the period to 2022 will be honoured but recognise that a range of other outcomes is possible, from re-running the auctions for delivery years 2019/2020, 2020/2021 and 2021/2022 to a significant revision of the structure of the Capacity Market. In each case, the exact impact of these changes cannot be predicted. However, the Directors note the UK Government's commitment to ensuring there is a capacity market in some form.

## **9. Working capital**

Drax is of the opinion that, taking into account the Acquisition Facility and other facilities available to the Enlarged Group, the Enlarged Group has sufficient working capital available to it for its present requirements, that is, for at least the next 12 months from the date of publication of this Circular.

<sup>4</sup> The UK Government's press release can be found at <https://www.gov.uk/government/collections/electricity-market-reform-capacity-market>.

<sup>5</sup> The published advice of National Grid in relation to the Capacity Market Ruling can be found at <https://www.emrdeliverybody.com/cm/home.aspx> and <https://www.emrdeliverybody.com/Prequalification/Advice%20for%20capacity%20agreement%20holders%20and%20capacity%20market%20applicants%20v1.1.pdf>.

## 10. Consents

J.P. Morgan Cazenove has given, and has not withdrawn, its consent to the inclusion in this Circular of the references to its name in the form and context in which they are included.

Deloitte LLP is registered to carry out audit work in the UK and Ireland by the Institute of Chartered Accountants in England and Wales and has given, and not withdrawn, its written consent to the inclusion of its report on historical financial information in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) and its report on the unaudited pro forma financial information in Part VI (*Unaudited Pro Forma Financial Information relating to the Enlarged Group*), in the form and context in which they are included.

## 11. Significant change

### 11.1 Drax

There has been no significant change in the financial or trading position of the Drax Group since 30 June 2018, being the date of the last financial period for which financial information has been published.

### 11.2 ScottishPower Generation Group

Except as provided below, there has been no significant change in the financial or trading position of the ScottishPower Generation Group since 31 December 2017, being the date to which the financial information on the ScottishPower Generation Group, presented in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*), has been prepared.

As disclosed in paragraph 6.2 of Part I (*Letter from the Chairman of Drax Group plc*), pursuant to the Capacity Market Ruling the Portfolio's contracted capacity payments for the 1 October 2018 to 31 December 2018 period have been suspended. These are expected to be around £12.7 million gross.

## 12. Related party transactions

Details of related party transactions (which for these purposes are those set out in the standards adopted according to Regulation (EC) No 1606/2002), which Drax has entered into:

- (A) during the financial year ended 31 December 2015 are disclosed in accordance with the respective standard adopted according to Regulation (EC) No 1606/2002 in note 8.4 on page 145 of Drax's 2015 Annual Report and Accounts;
- (B) during the financial year ended 31 December 2016 are disclosed in accordance with the respective standard adopted according to Regulation (EC) No 1606/2002 in note 8.4 on page 166 of Drax's 2016 Annual Report and Accounts; and
- (C) during the financial year ended 31 December 2017 are disclosed in accordance with the respective standard adopted according to Regulation (EC) No 1606/2002 in note 8.3 on page 171 of Drax's 2017 Annual Report and Accounts.

In respect of the period from 1 January 2018 to the date of this Circular, Drax's only related party transactions were the payment of salary and benefits to its Directors and Executive Committee members.

## 13. Source of financial information

Unless otherwise stated:

- (A) financial information relating to Drax has been extracted without material adjustment from Drax's 2017 Annual Report and Accounts; and
- (B) financial information relating to SPGEN has been extracted without material adjustment from the historical financial information set out in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*) and the audited financial statements of SPGEN for the years ended 2015, 2016 and 2017.

#### 14. Information incorporated by reference

Information from the following documents has been incorporated into this Circular by reference:

Documents containing information incorporated by reference	Paragraph of this Circular which refers to the document containing information incorporated by reference	Where the information can be accessed by Shareholders
Drax's 2015 Annual Report and Accounts	Paragraphs 5, 12 and 13 of this Part VIII	<a href="http://www.drax.com/investors/results-reports-agm">www.drax.com/investors/results-reports-agm</a>
Drax's 2016 Annual Report and Accounts	Paragraph 12 of this Part VIII	<a href="http://www.drax.com/investors/results-reports-agm">www.drax.com/investors/results-reports-agm</a>
Drax's 2017 Annual Report and Accounts	Paragraph 12 of this Part VIII	<a href="http://www.drax.com/investors/results-reports-agm">www.drax.com/investors/results-reports-agm</a>
Opus Circular	Paragraph 7.1 of this Part VIII	<a href="http://www.drax.com/wp-content/uploads/2017/01/Proposed-acquisition-by-Drax-Group-plc-of-Opus-Energy-Group-Limited-and-Notice-of-General-Meeting.pdf">www.drax.com/wp-content/uploads/2017/01/Proposed-acquisition-by-Drax-Group-plc-of-Opus-Energy-Group-Limited-and-Notice-of-General-Meeting.pdf</a>

A copy of each of the documents listed above is available for inspection in accordance with paragraph 15 below. The only part of the Opus Circular which is incorporated into this Circular is Part IV (*Principal Terms of the Acquisition*) of the Opus Circular. Parts of the Opus Circular which are not incorporated by reference are not relevant for the purposes of this Circular or are covered elsewhere in this Circular.

#### 15. Documents available for inspection

Copies of the following documents will be available for inspection at the offices of Drax at Drax Power Station, Selby, North Yorkshire YO8 8PH, United Kingdom and Slaughter and May at One Bunhill Row, London EC1Y 8YY, United Kingdom during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) up to and including the date of the General Meeting, and at the place of the General Meeting from 15 minutes prior to its commencement until its conclusion:

- (i) the articles of association of Drax;
- (ii) Drax's 2015 Annual Report and Accounts;
- (iii) Drax's 2016 Annual Report and Accounts;
- (iv) Drax's 2017 Annual Report and Accounts;
- (v) the Opus Circular;
- (vi) the report of Deloitte set out in Part V (*Historical Financial Information relating to the ScottishPower Generation Group*);
- (vii) the report of Deloitte set out in Part VI (*Unaudited Pro Forma Financial Information relating to the Enlarged Group*);
- (viii) the Acquisition Agreement and the Acquisition Agreement Amendment Deed;
- (ix) the consent letters of J.P. Morgan Cazenove and Deloitte referred to in paragraph 10 above;
- (x) this Circular; and
- (xi) the Drax announcement dated 16 October 2018 in relation to the Acquisition.

5 December 2018

## PART IX DEFINITIONS

The following terms have the following meanings in this Circular:

<b>“2018 Profit Forecast”</b>	means the statement in relation to the Drax Group set out in Part VII ( <i>Profit Forecasts</i> );
<b>“2019 Capacity Market Sensitivity Profit Forecast”</b>	means the statement in relation to the ScottishPower Generation Group set out in Part VII ( <i>Profit Forecasts</i> );
<b>“2019 Profit Forecast”</b>	means the statement in relation to the ScottishPower Generation Group set out in Part VII ( <i>Profit Forecasts</i> );
<b>“2022 Notes”</b>	means the £350 million aggregate principal amount of 4.250 per cent. Senior Secured Notes due 2022 issued on 5 May 2017 by Drax Finco under the 2022 Notes Indenture;
<b>“2022 Notes Indenture”</b>	means the Drax Finco indenture dated as of 5 May 2017, as amended and restated from time to time;
<b>“2025 Notes”</b>	means the US\$300 million aggregate principal amount of 6.625 per cent. Senior Secured Notes due 2025 issued on 26 April 2018 by Drax Finco under the 2025 Notes Indenture;
<b>“2025 Notes Indenture”</b>	means the Drax Finco indenture dated as of 26 April 2018, as amended and restated from time to time;
<b>“Acquisition”</b>	means the proposed acquisition of SPGEN pursuant to the Acquisition Agreement;
<b>“Acquisition Agreement”</b>	means the agreement dated 16 October 2018, between Drax Smart Generation and the Seller in relation to the Acquisition (as amended);
<b>“Acquisition Agreement Amendment Deed”</b>	means the deed dated 3 December 2018 amending the Acquisition Agreement between Drax Smart Generation and the Seller;
<b>“Acquisition Facility”</b>	means the £725 million committed acquisition facility under the Acquisition Facility Agreement;
<b>“Acquisition Facility Agreement”</b>	means the acquisition bridge facility agreement dated 16 October 2018 between Drax Corporate as borrower, Drax Group Holdings as original guarantor, Barclays Bank PLC, Bank of America Merrill Lynch International Limited and J.P. Morgan Securities plc as mandated lead arrangers, Barclays Bank PLC as facility agent, and Barclays Bank PLC, Bank of America Merrill Lynch International Limited and JPMorgan Chase Bank, N.A., London Branch as original lenders;
<b>“Board”</b>	means the board of Directors of Drax;
<b>“Brexit”</b>	means the forthcoming exit of the UK from the EU;
<b>“Capacity Market”</b>	means the UK Government initiative (established as part of the electricity market reform policy) to incentivise investment in more sustainable, low-carbon electricity capacity at the least cost for energy consumers;
<b>“Capacity Market Arrangement”</b>	means the arrangement included in the Acquisition Agreement Amendment Deed in response to the Capacity Market Ruling;

<b>“Capacity Market Ruling”</b>	means the ruling of the General Court of the European Union issued on 15 November 2018, annulling the European Commission’s 2014 decision not to undertake a more detailed investigation of the UK Government’s scheme establishing the Capacity Market;
<b>“CCGT”</b>	means combined cycle gas turbine stations, which generate electricity using both a gas turbine and a steam turbine;
<b>“Circular”</b>	means this document;
<b>“CMA”</b>	means the UK Competition and Markets Authority;
<b>“Companies Acts”</b>	has the meaning given in section 2 of the Companies Act 2006;
<b>“Company” or “Drax”</b>	means Drax Group plc, a public limited company incorporated in England and Wales with registered number 5562053 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Completion”</b>	means the completion of the purchase of the entire issued share capital of SPGEN pursuant to the Acquisition Agreement;
<b>“CREST”</b>	means the system of paperless settlement of trades in securities and the holding of uncertificated securities operated by Euroclear in accordance with the Uncertificated Securities Regulations 2001 (SI 2001/3755);
<b>“CREST Manual”</b>	means the manual, as amended from time to time, produced by CRESTCo describing the CREST system and supplied by CRESTCo Limited to users and participants thereof;
<b>“CREST Proxy Instruction”</b>	means the instruction whereby CREST members send a CREST message appointing a proxy for the meeting and instructing the proxy on how to vote;
<b>“Directors”</b>	means the directors of Drax;
<b>“Disclosure and Transparency Rules” or “DTRs”</b>	means the Disclosure Guidance and Transparency Rules made by the FCA pursuant to Part VI of FSMA;
<b>“Drax”</b>	means Drax Group plc, a public limited company incorporated in England and Wales with registered number 5562053 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax Corporate”</b>	means Drax Corporate Limited, a private limited company incorporated in England and Wales with registered number 05562058 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax Developments”</b>	means Drax Research and Innovation Holdco Limited (previously known as Drax Developments Limited), a private limited company incorporated in England and Wales with registered number 06657454 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax Finco”</b>	means Drax Finco plc, a public limited company incorporated in England and Wales with registered number 10664639 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;

<b>“Drax Group”</b>	means Drax and its subsidiary undertakings from time to time;
<b>“Drax Group Holdings”</b>	means Drax Group Holdings Limited, a private limited company incorporated in England and Wales with registered number 09887429 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax Power”</b>	means Drax Power Limited, a private limited company incorporated in England and Wales with registered number 04883589 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax Power Station”</b>	means Drax’s biomass and coal-fired power station in North Yorkshire, England;
<b>“Drax Smart Generation”</b>	means Drax Smart Generation Holdco Limited, a private limited company incorporated in England and Wales with registered number 07821911 and with its registered office at Drax Power Station, Selby, North Yorkshire YO8 8PH;
<b>“Drax’s 2015 Annual Report and Accounts”</b>	means the annual report and accounts prepared by Drax for the financial year ended 31 December 2015;
<b>“Drax’s 2016 Annual Report and Accounts”</b>	means the annual report and accounts prepared by Drax for the financial year ended 31 December 2016;
<b>“Drax’s 2017 Annual Report and Accounts”</b>	means the annual report and accounts prepared by Drax for the financial year ended 31 December 2017;
<b>“EBITDA”</b>	means earnings before interest, tax, depreciation, amortisation, unrealised gains and losses on derivative contracts and material or one-off items that do not reflect the underlying trading performance of the business;
<b>“Enlarged Group”</b>	means the Drax Group including the ScottishPower Generation Group after the Acquisition;
<b>“EU”</b>	means the European Union;
<b>“FCA”</b>	means the Financial Conduct Authority of the United Kingdom;
<b>“Fitch”</b>	means Fitch Ratings Inc.;
<b>“Form of Direction”</b>	means the form of direction accompanying this Circular (for Share Incentive Plan participants who have not elected to receive shareholder communications in electronic form) for use by Share Incentive Plan participants in connection with the General Meeting;
<b>“Form of Proxy”</b>	means the form of proxy accompanying this Circular (for those Shareholders who have not elected to receive shareholder communications in electronic form) for use by Shareholders in connection with the General Meeting;
<b>“FSMA”</b>	means the Financial Services and Markets Act 2000, as amended;
<b>“General Meeting”</b>	means the general meeting of Drax convened by the notice that is set out at the end of this Circular to be held at the offices of FTI Consulting, 200 Aldersgate Street, London EC1A 4HD on 21 December 2018 at 10.00am or any reconvened meeting following any adjournment thereof;



<b>“Guarantors”</b>	means the guarantors under the Acquisition Facility Agreement, which are Drax Group Holdings and certain subsidiaries of Drax Group Holdings;
<b>“IAS”</b>	means the International Accounting Standards;
<b>“IFRIC”</b>	means the interpretations of the IFRS Interpretations Committee;
<b>“IFRS”</b>	means the International Financial Reporting Standards;
<b>“Intercreditor Agreement”</b>	means the intercreditor agreement dated 5 May 2017 between, among others, Drax Corporate, Drax Finco, certain other subsidiaries of Drax Group Holdings and certain creditors of the Restricted Group;
<b>“Investment Contract”</b>	means an investment contract relating to Unit 1 with the Secretary of State for Energy and Climate Change;
<b>“J.P. Morgan Cazenove”</b>	means J.P. Morgan Securities plc (which conducts its UK investment banking activities as J.P. Morgan Cazenove);
<b>“Latest Practicable Date”</b>	means 3 December 2018, being the latest practicable date for the calculation and inclusion of information prior to the publication of this Circular;
<b>“LIBOR”</b>	means the London Interbank Offered Rate;
<b>“Listing Rules”</b>	means the Listing Rules made by the FCA pursuant to FSMA governing, inter alia, admission of securities to the Official List of the FCA;
<b>“London Stock Exchange”</b>	means the London Stock Exchange plc or any recognised investment exchange for the purposes of FSMA that may take over the functions of the London Stock Exchange plc;
<b>“Long Stop Date”</b>	means 30 April 2019;
<b>“Manweb Scheme”</b>	means the defined benefit Manweb Group of the Electricity Supply Pension Scheme;
<b>“New Scheme”</b>	means the new defined benefit pension scheme to be set up after an interim period by the ScottishPower Generation Group for the benefit of its employees;
<b>“NGET”</b>	means National Grid Electricity Transmission plc;
<b>“Notice”</b>	means the notice of General Meeting at Part X ( <i>Notice of General Meeting</i> );
<b>“O&amp;M”</b>	means operation and maintenance;
<b>“OCGT”</b>	means an open cycle gas turbine, which generates electricity using a gas turbine;
<b>“Opus Circular”</b>	means the circular dated 18 January 2017 relating to the acquisition by Drax of Opus Energy Group Limited;
<b>“Ordinary Shares”</b>	means ordinary shares of 11 <sup>16</sup> / <sub>29</sub> pence each in the capital of the Company;

<b>“Portfolio”</b>	means the portfolio of assets which is the subject of the Acquisition Agreement, consisting of Cruachan pumped storage hydro (440MW), run-of-river hydro locations at Galloway and Lanark (126MW), four CCGT stations, Damhead Creek (805MW), Rye House (715MW), Shoreham (420MW) and Blackburn Mill (60MW), and a biomass-from-waste facility (Daldowie);
<b>“Prudent Operating Practice”</b>	means the practices and the level of skill, care and diligence that would reasonably be expected of a skilled, experienced and prudent operator of a business of a similar size, nature and complexity to the business of SPGEN (or a relevant part of it);
<b>“Registrars”</b>	means Equiniti Limited, Proxy Department, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA;
<b>“Renewables Obligation”</b>	means the financial support mechanism for large-scale renewable electricity generation in the UK introduced in 2002;
<b>“Resolution”</b>	means the ordinary resolution as set out in the Notice of General Meeting at the end of this Circular;
<b>“Restricted Group”</b>	means Drax Group Holdings and its subsidiaries from time to time (save for any such subsidiaries which are designated as unrestricted subsidiaries from time to time in accordance with the terms of the Acquisition Facility Agreement, the Senior Facilities Agreement, the 2022 Notes Indenture and the 2025 Notes Indenture);
<b>“Revolving Facility”</b>	means the £315 million committed multicurrency working capital and ancillary facility, including, without limitation, a letter of credit facility provided under the Senior Facilities Agreement;
<b>“ROC”</b>	means a Renewables Obligation Certificate, a tradable certificate issued by Ofgem to an accredited generator for electricity generated from eligible renewable sources in the UK;
<b>“S&amp;P”</b>	means Standard & Poor’s Financial Services LLC;
<b>“ScottishPower Generation Group”</b>	means SPGEN and SMW;
<b>“Secured Trading Line”</b>	means the arrangement under ISDA agreements between Drax Power and a number of financial institutions, under which Drax Power can trade UK power, dark green spreads and gas on a senior secured basis without the requirement for Drax Power to post collateral;
<b>“Seller”</b>	means ScottishPower Generation Holdings;
<b>“Senior Facilities”</b>	means the Revolving Facility and the Term Loan;
<b>“Senior Facilities Agreement”</b>	means the revolving credit facility agreement dated 20 December 2012 between, among others, Drax Power as borrower, Barclays Bank PLC as facility agent and Drax Corporate, as amended and restated pursuant to an amendment and restatement agreement on 21 April 2017, with effect from 5 May 2017;
<b>“Share Incentive Plan”</b>	means the Drax Group Approved Share Incentive Plan;
<b>“Shareholders”</b>	means holders of Ordinary Shares;

<b>“SMW”</b>	means SMW Limited, a private limited company incorporated in Scotland with registered number SC165988 and with its registered office at 320 St. Vincent Street, Glasgow, Scotland, G2 5AD;
<b>“SPGEN”</b>	means ScottishPower Generation Limited, a company incorporated in Scotland with registered number SC189124, whose registered office is at 320 St. Vincent Street, Glasgow, Scotland, G2 5AD;
<b>“SPPS”</b>	means the defined benefit ScottishPower Pension Scheme;
<b>“subsidiary” and “subsidiary undertaking”</b>	have the meanings given to them in sections 1159 and 1162 (respectively) of the Companies Act 2006;
<b>“Term Loan”</b>	means the £35 million term facility provided under the Senior Facilities Agreement;
<b>“Transitional Services Agreement” or “TSA”</b>	means the transitional services agreement to be entered into at Completion between Drax Smart Generation and the Seller;
<b>“Unaudited Pro Forma Financial Information”</b>	means the unaudited pro forma income statement and unaudited pro forma net assets statement of the Enlarged Group set out in Part A in Part VI; and
<b>“Unit 1”</b>	means Drax Power’s third coal-to-biomass conversion unit.

**PART X  
NOTICE OF GENERAL MEETING**

**Drax Group plc**

*(Registered in England and Wales with registered number 5562053)*

**NOTICE IS HEREBY GIVEN** that a General Meeting of Drax Group plc (the “**Company**”) will be held at the offices of FTI Consulting, 200 Aldersgate Street, London EC1A 4HD on 21 December 2018 at 10.00am to consider and, if thought fit, to pass the following resolution as an ordinary resolution of the Company:

**Ordinary Resolution**

THAT the proposed acquisition of the entire issued share capital of ScottishPower Generation Limited (the “**Transaction**”) on the terms and subject to the conditions of a sale and purchase agreement dated 16 October 2018 (as amended on 3 December 2018) between (1) Scottish Power Generation Holdings Limited, and (2) Drax Smart Generation HoldCo Limited and summarised in the circular dated 5 December 2018 relating to the Transaction be and is hereby approved, and any and all of the directors of the Company be and are hereby authorised to: (i) do all such acts and things and execute all such agreements and make such arrangements as they may consider to be necessary, desirable or appropriate to complete, implement and to give effect to, or otherwise in connection with, the Transaction and any matters incidental to the Transaction; and (ii) waive, amend, vary, revise or extend any of the terms and conditions of such agreements, provided that any such waivers, amendments, revisions or extensions are not of a material nature.

By order of the Board

David McCallum  
General Counsel and Group Company Secretary  
Drax Group plc

5 December 2018

Notes:

1. Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001 (as amended) and for the purposes of section 360B of the Companies Act 2006 (“CA 2006”), the Company specifies that only those shareholders registered on the register of members of the Company (“Register”) at 6.30pm on the day two business days before the date of the meeting (the “Specified Time”) (or if the meeting is adjourned to a time more than 48 hours after the Specified Time, by 6.30pm on the day which is two business days prior to the time of the adjourned meeting) shall be entitled to attend and vote thereat in respect of the number of shares registered in their name at that time. If the meeting is adjourned to a time not more than 48 hours after the Specified Time, that time will also apply for the purposes of determining the entitlement of members to attend and vote (and for the purposes of determining the number of votes they may cast) at the adjourned meeting. Changes to the Register after the relevant deadline shall be disregarded in determining rights to attend and vote.
2. If you have sold or transferred all your shares, this Circular and any accompanying documents (but not the personalised Form of Proxy or Form of Direction) should be passed to the person through whom the sale or transfer was made for transmission to the purchaser or transferee.
3. If you are a member of the Company, at the time set out in note 1 above, you are entitled to appoint one or more proxies to exercise all or any of your rights to attend, speak and vote at the meeting. Completion and return of a Form of Proxy will not prevent a member from attending in person and voting at the meeting. If a member appoints more than one proxy to attend the meeting, each proxy must be appointed to exercise the rights attached to a different share or shares held by that member.

If a member wishes to appoint more than one proxy and so requires additional proxy forms, the member should contact the Company’s Registrars, Equiniti Limited, Proxy Department, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA or by using their telephone helpline service on 0371 384 2030 from within the UK. Lines are open from 8.30am to 5.30pm, Monday to Friday – excluding Bank Holidays; or +44 121 415 7047 from outside the UK.

4. A proxy does not need to be a shareholder of the Company but must attend the meeting for the member’s vote to be counted. Your proxy could be the Chairman, another director of the Company or another person who has agreed to attend to represent you. Details of how to appoint the Chairman or another person (or persons) as your proxy using the Form of Proxy are set out in the notes to the Form of Proxy. Appointing a proxy does not preclude you from attending the meeting and voting in person.
5. You can only appoint a proxy using the procedures set out in these notes and the notes on the Form of Proxy. A Form of Proxy is enclosed. To be effective, the Form of Proxy must be completed and signed and, together with the power of

attorney or authority, if any, under which it is signed (or a duly certified copy of any such power or authority), must be lodged with the Company's Registrars not later than 48 hours, excluding non-business days, before the time of the meeting or must be lodged using the CREST proxy voting services (see note 7 below). Return of a completed Form of Proxy will not preclude a member from attending and voting personally at the meeting.

6. In the case of joint holders, where more than one of the joint holders purports to appoint a proxy, only the appointment submitted by the most senior holder will be accepted. Seniority is determined by the order in which the names of the joint holders appear in the Register in respect of the joint holding (the first-named being deemed the most senior).
7. CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so for the meeting and any adjournment(s) thereof utilising the procedures described in the CREST Manual (available via [www.euroclear.com](http://www.euroclear.com)). CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf. In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a CREST Proxy Instruction) must be properly authenticated in accordance with Euroclear UK & Ireland Limited's specifications and must contain the information required for such instructions, as described in the CREST Manual.

The message, regardless of whether it constitutes the appointment of a proxy or an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the Company's agent, Equiniti Limited (CREST participant ID RA19) by the latest time(s) for receipt of proxy appointments specified in note 5 above. For this purpose the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the Company's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

CREST members and, where applicable, their CREST sponsors or voting service providers should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular messages. Normal system timings and limitations will therefore apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member or sponsored member or has appointed a voting service provider(s), to procure that his or her CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time.

In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings available at [www.euroclear.com](http://www.euroclear.com).

The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in regulation 35(5)(a) of the Uncertificated Securities Regulations 2001 (as amended).

8. A vote withheld is not a vote in law, which means that the vote will not be counted in the calculation of votes for or against the Resolution. If you either select the "discretionary" option or if no voting indication is given, your proxy will vote or abstain from voting at his or her discretion. Your proxy will vote (or abstain from voting) as he or she thinks fit in relation to any other matter which is put before the meeting.
9. If the Chairman, as a result of any proxy appointments, is given discretion as to how the votes the subject of those proxies are cast and the voting rights in respect of those discretionary proxies, when added to the interests in the Company's securities already held by the Chairman, result in the Chairman holding such number of voting rights that he has a notifiable obligation under the Disclosure and Transparency Rules, the Chairman will make the necessary notifications to the Company and the Financial Conduct Authority. As a result, any member holding 3 per cent. or more of the voting rights in the Company who grants the Chairman a discretionary proxy in respect of some or all of those voting rights and so would otherwise have a notification obligation under the Disclosure and Transparency Rules, need not make a separate notification to the Company and the Financial Conduct Authority.
10. If you are not a member of the Company but you have been nominated by a member of the Company to enjoy information rights, you do not have a right to appoint any proxies under the procedures set out in notes 3 to 9. Please read note 15 below.
11. Alternatively, members may register the appointment of a proxy for the meeting electronically by accessing the website [www.sharevote.co.uk](http://www.sharevote.co.uk) where full details of the procedure are given. This website is operated by the Company's Registrars.

The proxy appointment and any power of attorney or other authority under which the proxy appointment is made must be received by the Company's Registrars not less than 48 hours, excluding non-business days, before the time for holding the meeting or adjourned meeting or (in the case of a poll taken otherwise than at or on the same day as the meeting or adjourned meeting) for the taking of the poll at which it is to be used. Please note that any electronic communication sent to the Company or to the Company's Registrars that is found to contain a computer virus will not be accepted. The use of the internet service in connection with the General Meeting is governed by the Company's Registrars' conditions of use set out on the Sharevote website, [www.sharevote.co.uk](http://www.sharevote.co.uk), and may be read by logging on to that site. If you want to appoint more than one proxy electronically please contact the Company's Registrars on 0371 384 2030 from within the UK. Lines are open from 8.30am to 5.30pm, Monday to Friday – excluding Bank Holidays; or +44 121 415 7047 from outside the UK.

12. A copy of this Notice and other information required by section 311A of the CA 2006 can be found on the Company's website [www.drax.com](http://www.drax.com).
13. To change your proxy instructions, simply submit a new proxy appointment. You will need to request a new Form of Proxy from the Company's Registrars, Equiniti Limited, by contacting them at Equiniti Limited, Proxy Department, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA or by using their telephone helpline service on 0371 384 2030 from within the UK. Lines are open from 8.30am to 5.30pm, Monday to Friday – excluding Bank Holidays; or +44 121 415 7047 from outside the UK. Note that the cut-off time for receipt of Forms of Proxy (see note 5 above) also applies in relation to

amended instructions; any amended proxy appointment received after the relevant cut-off time will be disregarded and you will be required to vote at the meeting, if you wish to change your vote.

14. If you submit more than one valid proxy appointment in respect of a single share, the appointment received last before the latest time for the receipt of proxies will take precedence.
15. Any person receiving a copy of this Notice as a person nominated by a member to enjoy information rights under section 146 of the CA 2006 (a "Nominated Person") should note that the provisions in this Notice concerning the appointment of a proxy or proxies to attend the meeting in place of a member do not apply to a Nominated Person as only shareholders have the right to appoint a proxy. However, a Nominated Person may have a right under an agreement between the Nominated Person and the member by whom he or she was nominated to be appointed, or to have someone else appointed, as a proxy for the meeting. If a Nominated Person has no such proxy appointment right, or does not wish to exercise it, he or she may have a right under such an agreement to give instructions to the member as to the exercise of voting rights at the meeting. If you are a person who has been nominated under section 146 of CA 2006 to enjoy information rights:
  - you may have a right under an agreement between you and the member of the Company who has nominated you to have information rights (a "Relevant Member") to be appointed or to have someone else appointed as a proxy for the meeting; and
  - if you either do not have such a right or if you have such a right but do not wish to exercise it, you may have a right under an agreement between you and the Relevant Member to give instructions to the Relevant Member as to the exercise of voting rights. Nominated Persons should also remember that their main point of contact in terms of their investment in the Company remains the member who nominated the Nominated Person to enjoy information rights (or the custodian or broker who administers the investment on their behalf). Nominated Persons should continue to contact that member, custodian or broker (and not the Company) regarding any changes or queries relating to the Nominated Person's personal details and interest in the Company (including any administrative matter). The only exception to this is where the Company expressly requests a response from a Nominated Person.
16. Voting on the Resolution to be put to the General Meeting will be by poll, rather than a show of hands, so that all shares voted are included, whether or not the shareholder is able to attend the meeting. The board of directors of the Company believes this to be the most democratic procedure for voting on resolutions as member votes will be counted according to the number of shares held.

The results of the voting at the meeting and the number of proxy votes cast for and against and the number of votes actively abstained in respect of the Resolution proposed at the meeting will be announced to the London Stock Exchange as soon as practicable following the meeting and also will be published on the Company's website, [www.drax.com](http://www.drax.com).
17. As at 3 December 2018, being the latest practicable date prior to the publication of this Notice, the Company's issued share capital comprised 407,185,287 ordinary shares of 11<sup>16</sup>/<sub>29</sub> pence each. Each ordinary share carries the right to one vote at a general meeting of the Company and the Company held 11,851,542 shares in treasury as at 3 December 2018. Therefore, the total number of voting rights in the Company as at 3 December 2018 was 395,333,745.
18. This Notice, together with information about the total numbers of shares in the Company in respect of which members are entitled to exercise voting rights at the meeting as at 3 December 2018, being the latest practicable date prior to the publication of this Notice and, if applicable, any members' statements, members' resolutions or members' matters of business received by the Company after the date of this Notice, will be available on the Company's website, [www.drax.com](http://www.drax.com).
19. Any corporation which is a member can appoint one or more corporate representatives who may exercise on its behalf all of its powers as a member provided that it does not do so in relation to the same shares.
20. Any member attending the meeting has the right to ask questions. The Company must cause to be answered any question relating to the business being dealt with at the meeting put by a member attending the meeting. However, members should note that no answer need be given in the following circumstances:
  - if to do so would interfere unduly with the preparation of the meeting or would involve a disclosure of confidential information;
  - if the answer has already been given on a website in the form of an answer to a question; or
  - if it is undesirable in the interests of the Company or the good order of the meeting that the question be answered.
21. Any electronic address provided either in this Notice or in any related documents (including the Form of Proxy) may not be used to communicate with the Company for any purposes other than those expressly stated.
22. The doors of the General Meeting venue will open at 9.30am and the General Meeting will start promptly at 10.00am. Please bring the attendance card which is attached to the Form of Proxy with you if you attend the meeting. It will authenticate your right to attend, speak and vote and will speed up your admission to the meeting.
23. You may be asked to provide proof of identity, as well as your attendance card from your Form of Proxy. If you do not have your attendance card, you may be asked to provide two forms of identity (which may require photo identity and verification of your address). If you have been appointed as proxy for a shareholder entitled to vote, please let the admission staff know. You should bring proof of identity with you and you will be asked to confirm the details of the shareholder you are representing.
24. If you have any queries about voting or about your shareholding, you can contact Equiniti Limited, who maintain the Register, as follows:
  - by using their telephone helpline service:
    - from within the UK, on 0371 384 2030; or
    - from outside the UK, on +44 121 415 7047; or
  - by writing to them at Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA.

The helpline for Share Incentive Plan participants is: UK 0371 384 2040, overseas +44 121 415 7161.

The telephone helpline service will be available between 8.30am and 5.30pm, Monday to Friday – excluding Bank Holidays.

The telephone helpline service will not be able to provide legal, financial or personal taxation advice. Calls may be recorded and randomly monitored for security and training purposes.

25. The Company considers it beneficial to its shareholders to hold the General Meeting as soon as possible in order to allow it to, assuming shareholders vote in favour of the Resolution, assume control of ScottishPower Generation Limited and begin to integrate the two businesses and obtain the other benefits of ownership of ScottishPower Generation Limited. As a result, the Company has not given 14 working days' notice of the General Meeting as provided for in the guidance given by paragraph E.2.4 of the UK Corporate Governance Code. The Company is, however, fully compliant with the legal requirements of the CA 2006 and its articles of association, having given 14 days' clear notice of the General Meeting.

