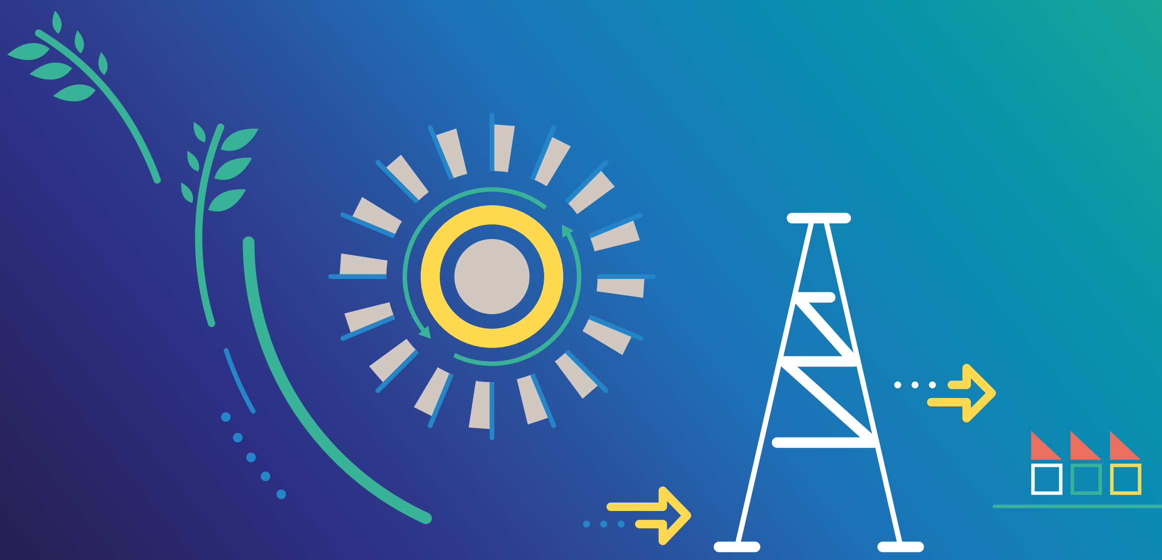
SMART ENERGY SOLUTIONS

Drax Group plc
Annual report and accounts
2016



drax

Smart energy solutions for today's and tomorrow's challenges.

For more than a decade, Drax Group plc has been leading the world in developing the technology and capacity to provide flexible, reliable and affordable generation and supply of electricity from sustainable biomass.

The flexibility that our biomass provides makes us the perfect partner for intermittent renewables, plugging the gaps when the sun doesn't shine and the wind doesn't blow.

Drax continues to explore options to deliver targeted long-term growth, evaluating opportunities across the markets in which we operate – pellet supply, generation and retail. Our strategy will deliver greater diversification for the business as it helps change the way energy is generated, supplied and used for a better future.

Smart sourcing: Drax transforms underutilised low-grade wood into high-quality compressed wood pellets. Our strategy is to expand our self-supply of sustainable biomass.

Smart generation: We use this fuel to produce a reliable supply of low-carbon renewable electricity from our upgraded power station. We also operate flexible coal-fuelled units and plan to develop four rapid-response gas generation plants.

Smart supply: Drax provides renewable electricity to businesses and helps keep the UK electricity supply secure. We're always working to develop new technologies.

STRATEGIC REPORT

GOVERNANCE

FINANCIALS

2016 Highlights

£2,950M

Total revenue
(2015: £3,065 million)

£376M

Gross profit
(2015: £409 million)

£93M

Net debt
(2015: £187 million)

£140M

EBITDA(1)
(2015: £169 million)

5P

Underlying basic earnings per share(1)
(2015: 11p)

0.22

Total recordable injury rate
(2015: 0.31)

16%

Percentage of total UK renewable electricity generated(2)
(2015: 16%)

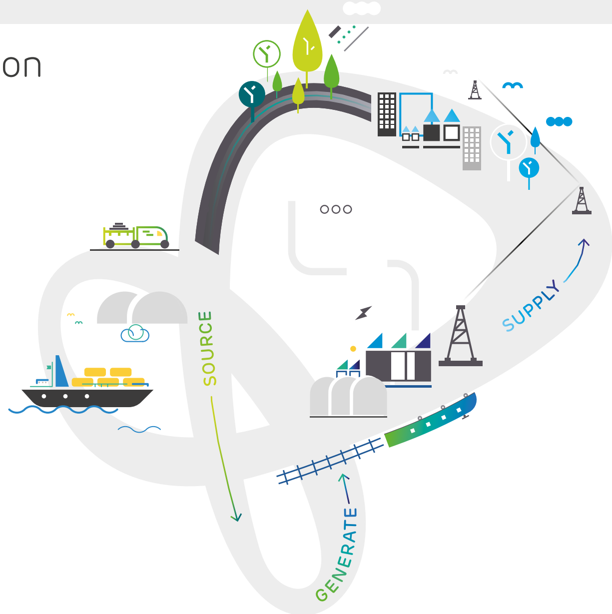
65%

Percentage of Drax's electricity generated by sustainable biomass
(2015: 43%)

(1) See page 118.
(2) Drax estimates that it produced around 16% of the renewable electricity generated under support schemes covered by the Levy Control Framework.

WHAT'S INSIDE?

Discover the diversification of Drax Group, which enables us to source, generate and supply reliable, renewable and affordable electricity.



drax biomass

SMART SOURCING

Drax Biomass is a world-class provider of compressed wood pellets from sustainably managed forests.

We take low-grade wood and transform it into high-quality pellets that can be transported safely and efficiently around the world to supply reliable, flexible and affordable low-carbon energy.

900,000

Our two pellet processing plants in the USA can produce 900,000 metric tonnes of compressed wood pellets every year.

PG.12

drax power

SMART GENERATION

Drax Power generates around 7% of the UK's electricity needs – reliably and affordably. We also sell our power through the UK wholesale electricity markets.

In 2016, Drax Power produced 16% of the UK's total renewable electricity – playing a vital role in ensuring stability, security of supply and the transition to a low-carbon future.

16%

We have the flexibility to help meet electricity demand when intermittent renewables like solar or wind power cannot generate.

PG.16

haven power

SMART SUPPLY

Haven Power supplies electricity to businesses. Billington Bioenergy supplies sustainable compressed wood pellets to provide businesses and households with renewable heat.

Haven offers customers 100% renewable electricity, competitive pricing and contracts tailored precisely to their needs. We were named Supplier of the Year at the 2016 Energy Awards.

14.6TWH

Haven Power increased 2016 power sales from 13.8TWH in 2015.

PG.20

Our sustainability policy is at the heart of our business. Read about our sustainability principles.

PG.36

Group CEO, Dorothy Thompson shares Drax Group's strategic direction in her overview of 2016.

PG.06

CHAIRMAN'S STATEMENT

GROUP STRATEGY

HIGHER QUALITY DIVERSIFIED EARNINGS AND MANAGEMENT OF COMMODITY MARKET EXPOSURE	– Increased contractual and non-commodity related earnings – Broader and more diversified earnings
TARGETING LONG-TERM GROWTH	– Identify opportunities for post-2027 earnings – Creating new opportunities in all the markets in which we operate
OPERATIONAL EXCELLENCE	– Building on existing strengths

SMART SOURCING
- At least 20–30% biomass self-supply
- New biomass markets

SMART GENERATION
- Diversified generation and capacity
- Flexible, reliable operations and contract-based revenues

SMART SUPPLY
- Profitable business with critical mass

2016 was a pivotal year for Drax, marking the completion of the biomass transformation project which commenced in 2012, and the announcement of a new strategy to deliver long-term sustainable value.

Against a background of low wholesale electricity prices, and a volatile and demanding environment for renewable energy providers, the Group has again delivered strong operational performance.

CREATING LONG-TERM VALUE FROM A DIVERSIFIED BASE

In 2016 a key focus for the Board was the development of a new strategy for the Group, in order to ensure we are well placed to create long-term value across all three segments of the business: smart upstream sustainable pellet manufacturing, smart power generation and smart retail.

Following a comprehensive review, initiated in 2015, the Group's new strategy has been defined and is based on creating a more diversified earnings base that will produce higher-quality returns in the long term. Central to this strategy, Drax aims to play an increasing role in delivering a robust low-carbon energy system for the UK.

We announced our new strategy to the market in December. Evidence of delivering on the new strategy can already be seen in the acquisition of Opus Energy and four projects to construct fast-response Open Cycle Gas Turbine (OCGT) generation plants.

RESULTS AND DIVIDEND

Our EBITDA for 2016 at £140 million was in line with our guidance, although below 2015 (£169 million). This result principally reflects very challenging commodity markets and the removal of Climate Change Levy (CCL) exemptions. However, we were able to partly offset the impact of these factors with a focus on flexible system support, the prompt and balancing markets, ancillary services and improving retail margins, all of which are important parts of our strategy to develop broader, non-commodity exposed earnings.

In accordance with our dividend policy, the Board proposes to pay a final dividend in respect of 2016 of 0.4 pence per share, equal to £1.8 million. This would give total dividends for the year of £10 million (2015: £23 million).

Given the evolution at our business, the Board believes that it is appropriate to review our dividend policy. Discussions with our shareholders will take place in the first half of 2017.

"DRAX IS WELL PLACED TO PROFIT FROM A CHANGING ELECTRICITY MARKET, AND TO DELIVER LONG-TERM, HIGH-QUALITY DIVERSIFIED EARNINGS.

14.6TWH

Sold to business customers

65%

Total of our electricity production generated from renewables

607,000 TONNES

Compressed wood pellets produced

POLITICAL AND REGULATORY

The Government's decision to apply the CCL to renewables continued to have a significant effect on our results, reducing EBITDA by an estimated £34 million in 2016. On a much more positive note, following an exhaustive and rigorous process, the European Commission approved our Contract for Difference (CfD).

2016 was a year of significant change for the UK Government, not least with the Brexit vote and its implications. Our strategy of long-term hedging against currency fluctuations ensured we were protected against a negative impact on the cost of our predominantly US dollar and Euro denominated biomass supply.

A new Prime Minister, a newly created department in the Department for Business, Energy and Industrial Strategy (BEIS), and changes to their respective teams mean new opportunities to make the case for further biomass upgrades at Drax. Our aim for the power station is to deliver 100% sustainable, renewable and reliable biomass generation.

Continuing to demonstrate the affordability of biomass is also critical, and an independent report commissioned by Drax in early 2016 showed that biomass is the lowest cost, scale, renewable generation available[1] – once total system costs have been accounted for.

CRITICAL ROLE TO PLAY IN THE ELECTRICITY MARKET

Drax has a major role to play, not just producing electricity when it is needed, but also in securing the stability of the electricity grid. We are a generator that combines flexibility, reliability and sustainability. Our unique profile enables us to help National Grid provide power whenever it is needed. We renewed our contract with National Grid to provide support services, and there are clearly greater opportunities for Drax to support the UK energy system in the future.

Drax's four planned rapid-response OCGT plants have the potential to provide the flexible and reliable electricity that the UK's homes and businesses will need in the years to come.

Changes in the retail energy market mean there are now greater opportunities for challenger brands to succeed. The acquisition of Opus Energy, with its strong track record of supplying power to small to medium-size businesses, will complement our existing offering from Haven Power, which is well established in the large commercial and industrial sector.

CORPORATE GOVERNANCE

Drax remains committed to the highest standards of corporate governance. The Board and its committees play an active role in guiding the Company and leading its strategy, which is why we are determined to ensure we have the right skillset to steer the Group forward.

We are strong advocates of diversity – in terms of thinking, background and gender.

In the course of 2016, Melanie Gee left the Board. I would like to thank her for her years of commitment and service as a non-executive director. We are actively seeking new non-executive directors whose skills will help us determine and deliver our strategy for long-term value. In this context, retail and sustainability are our primary focus.

Full details of our corporate governance can be found on page 62.

OUR PEOPLE

Finally, I must thank all the employees and contractors who have worked so hard to help Drax succeed in the last 12 months. As I said, it has continued to be an extremely busy period for everyone across all of our business, yet our team has once again pulled together to help us meet all of those challenges. We are privileged to have colleagues from such a diverse range of backgrounds and skills.

What we all share is the determination to do things in a sustainable way, and to continue to help the UK reduce its carbon emissions while continuing to provide the power our country requires.

It only remains for me to say that your Board remains totally committed to the complementary aims of delivering sustainable long-term value for the Drax business, and of helping our country build a low-carbon future through smart energy solutions.

Philip Cox CBE
Chairman

(1) nera.com/publications/archive/2016/NERA_Imperial_Feb_2016_Renewable_Subsidies_and_Whole_System_Costs_FINAL_160215.html

Q&A WITH THE CEO

Group CEO, Dorothy Thompson, answers the key questions that have been put to her by shareholders in 2016.

Q. DO YOU THINK PERFORMANCE GOT BETTER OR WORSE IN 2016?
A. Financially, EBITDA was in line with our guidance, although below 2015. This principally reflects very challenging commodity markets and the removal of the Climate Change Levy exemption.

We were able to partly offset the impact of these factors with a focus on flexible system support, in the prompt and balancing markets, ancillary services and improving retail profitability, all of which are important parts of our strategy to develop broader, non-commodity exposed earnings.

Operationally, 2016 was another good year across our business, but particularly in generation where the team completed a significant outage programme and on the regulatory front the European Commission's approval of the CfD meant we could complete the final stages of the upgrade to our third biomass unit.

Q. WHAT WERE THE MOST SIGNIFICANT CHANGES FOR THE GROUP IN 2016?
A. The most important change was the new Group strategy, which gives us all a very clear direction for the future and will see Drax become a broader business across our markets – pellet supply, generation and retail. The acquisition of Opus Energy will strengthen our retail offer, and our plans to build four rapid response gas power stations will plug the gaps at times of system stress.

The new Group strategy is underpinned by new people and IT strategies which are crucial to its successful delivery.

Haven Power has also seen significant change with the arrival of CEO Jonathan Kini. He, along with his team have been working to ensure we are well placed to continue growing and to boost our retail offer with the recent acquisition of Opus.

Q. HOW DO YOU THINK 2017 WILL BE DIFFERENT TO 2016?
A. The focus will be on continuing to deliver good performance right across the Group, but there will also be changes as we work closely with the Opus team to ensure we create the best possible retail offer for the UK's SMEs. Drax Power will be progressing the OCGT gas projects, and it will be an exciting year for Drax Biomass as they look to secure acquisitions of pellet mills and opportunities to export compressed word pellets to other markets. Everyone across the Group will see further evidence of the new strategy roll-out, particularly in the form of the people and IT strategies.

Q HOW DOES DIVERSIFYING INTO GAS FIT WITH YOUR AIM TO REPLACE COAL WITH RENEWABLE GENERATION AT DRAX?
A. It complements it perfectly. The European Commission's approval of the CfD enabled us to complete the upgrade of half the power station to run on compressed wood pellets in place of coal and in 2016, 65% of the electricity we generated at Drax was renewable.

The job is not yet done, and with the right conditions we will upgrade the remaining coal units. We can do this in just two to three years, when the conditions are right.

The planned gas power stations will not be run to produce baseload power, but as rapid response units to plug the gaps at times of system stress, for example when wind and solar fail to contribute what's required. They will also be part of a solution that can accelerate the end of coal in the UK.

Q. CAN YOU EXPLAIN THE ACQUISITION OF OPUS? WOULDN'T IT HAVE MADE MORE SENSE TO GROW HAVEN?
A. We acquired Haven in 2009 when it was an SME focused business. Since then the business has grown significantly by principally focusing on the I&C market to provide a route to market for around half the electricity Drax Power produces, although it retains a relatively small SME presence.

Opus – like Haven – is a challenger business and brings with it 265,000 customer metered sites, largely SMEs. Opus also supplies gas, which for the first time will see us having the ability to provide a dual fuel offer, something that is vital for many SMEs.

Opus gives us immediate scale in the SME market and we think the complementary nature of the Haven and Opus models can provide a compelling challenger retail proposition for our customers.

Q. HAVE YOU GOT THE RIGHT TEAM AND SYSTEMS IN PLACE TO ENSURE THAT OPUS WILL JOIN THE GROUP WITH MINIMAL DISRUPTION?

A. Yes, Jonathan Kini, who leads our retail business has a great depth of experience in SME markets and integration. He has strengthened his team to ensure we have the expertise required to make this a very successful transition as Opus becomes a member of the Drax family.

However, I'm in no way complacent about the challenges, that's why we developed a plan to embed Opus covering everything from IT to communications. It's vital we get this right and that our new colleagues become part of delivering our new Group strategy and share in our values. Clearly I also want both Haven and Opus customers to continue experiencing high levels of service along with the benefits of a more comprehensive retail offer.

Q. HOW IS DRAX POWER DIFFERENT TO WHEN YOU JOINED?

A. In many ways Drax is now a very different place to what it was when I joined Drax more than ten years ago. The fact that in 2016 65% of our output was renewable is something I'm very proud of, and right across the power station you can actually see the difference that using compressed wood pellets has made: huge storage domes, specially designed train wagons, and a visitor centre and guides explaining the latest chapter in the Drax story.

Essentially today the power station operates as two power stations: a reliable, flexible, renewable generator producing electricity for businesses and homes and a fossil fuel generator providing system support and security of supply.

Q. YOU HAVE HIGHLIGHTED THE ROLE THAT DRAX COAL UNITS CAN PLAY IN SYSTEM SUPPORT AND ANCILLARY SERVICES – WHAT IS THIS AND WHY IS IT IMPORTANT?

A. Increasing levels of intermittent renewables and inflexible nuclear present the grid with a challenge, and for Drax, opportunities.

When the grid needs capacity our coal units have the flexibility to turn on and off, and ramp up and down responding to demand as weather and time of day determine the availability of wind and solar. It is already common place for Drax to "two-shift" the coal units; using them to provide flexible, responsive power, rather than baseload.

But it's not just about generation – a well-functioning grid needs other services too. 2017 will see Drax seeking further opportunities to provide the electricity grid with this increasingly important system support.

Q. DID THE RESULT OF THE UK'S EU REFERENDUM HAVE ANY IMPACT ON THE BUSINESS?

A. Our business model is largely unaffected by the decision to leave the EU. We will continue to generate and sell power in the UK. We purchase a significant amount of the fuel we require in foreign currency and our long-term hedging strategy – five years ahead – has protected us against any negative impacts of exchange rate fluctuations for the medium-term.

Q. HAS THE CHANGE IN THE UK GOVERNMENT RESULTED IN ANY DIFFERENT SIGNALS BEING SENT OUT TO THE RENEWABLES SECTOR?

A. I think that still remains to be seen. We have to look at the huge changes that have happened in Government since the EU referendum as a potential opportunity for us as we continue to make the case for investment in further biomass upgrades.

What is clear is that the focus is still very much on affordable energy. In 2016, Imperial College London and the economic consultancy NERA published new research that we commissioned. It showed that when whole system costs are factored in biomass is the cheapest large scale renewable technology. If Government applied this method of support to future CfD auctions, consumers could benefit by up to £2.2 billion.

As we take forward our new strategy we will also be clearly communicating our plans for rapid response gas power stations and how the system support they will provide contributes to decarbonising the UK's energy system.

Q. WHAT ARE THE LATEST PLANS TO CONVERT THE REMAINING GENERATING UNITS THAT RUN ON COAL?

A. We have now delivered on our original strategy to upgrade three generating units to run on compressed wood pellets. However, we would like to do more, and have consistently said that with the right conditions we stand ready to convert further units.

The transformation we've been through has meant we've learnt a huge amount over the last few years, and there's no doubt that for future upgrades we can carry them out quicker and more cost-effectively.

Q. WHY DO YOU THINK QUESTIONS AROUND THE SUSTAINABILITY OF BIOMASS CONTINUE TO BE RAISED?

A. I think many companies involved in the sourcing and supply of sustainable products will face questions in this area. What we will do is continue to be open and honest about all aspects of how our business operates including sustainability. Much of that evidence can be seen in this annual report, from our own stringent sustainability policy, to how we comply with the UK Government's sustainability legislation criteria.

However, we are never complacent and for example each new pellet supplier to Drax is fully and independently audited before a contract is signed and our existing suppliers are audited at least once every three years.

Q. WHICH OTHER BUSINESS ROLES DO YOU HAVE OUTSIDE OF DRAX AND HOW DO THEY HELP THE GROUP?

A. I'm a non-executive director at the Eaton Corporation and also the Court of the Bank of England. I think it's important to have roles outside the business, as long as they allow you to get the balance right and these do. So, clearly they should in no way be a distraction from the "day job", but worth an investment of time that allows you to see how others operate and whether there are lessons that we can learn or best practice that we can adopt.

Q. WHAT'S THE FEELING AROUND THE BOARD TABLE?

A. I'd say it's one of excitement at the opportunities our new Group strategy and acquisitions present for the future. While there's obviously satisfaction that we've delivered on what we initially set out to do – upgrade three generating units to run on compressed wood pellets, there is certainly no feeling of "job done".

In the months ahead the Board will rightly want to see clear and positive progress as we work to boost our retail offer through Opus Energy and develop our plans to build four rapid response gas power stations.

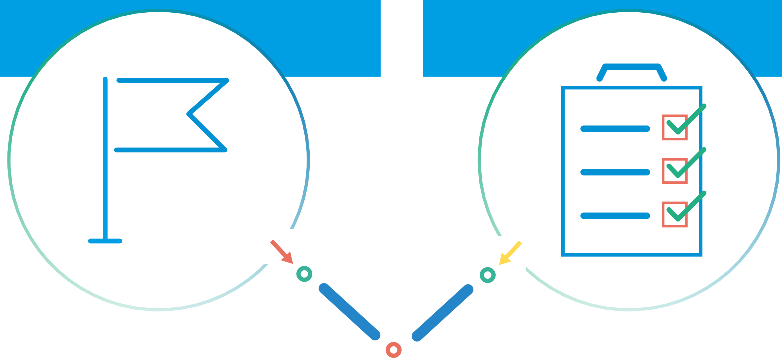
2016 began with some of the most challenging power and commodity markets I have seen in my career and in a similar way to 2015 this created a headwind to profitability.

PURPOSE

To help change the way energy is generated, supplied and used for a better future.

HOW

By providing inspiring, flexible energy solutions that make a difference to customers.



Operationally, performance across the Group has been good.

The strong operational performance across our business helped us to respond to the financial challenge posed by the difficult commodity markets and the removal of CCL exemptions. This enabled us to deliver EBITDA for 2016 at £140 million, in line with our guidance, but still below 2015 (£169 million). There is more detail on our financial performance in the Group Financial Review on page 50.

In response to the challenging commodity market conditions we evolved the operation of our coal units to provide increasingly important flexible system support services to the power grid, whilst at the same time our biomass units delivered a record level of renewable electricity.

In the US our pellet plants operated well. During the year we used the flexibility of self-supply to manage production to allow the Group to benefit from attractively priced biomass cargoes in the short-term spot market.

In Retail, Haven Power has delivered a good performance with volumes at scale and improved gross margin.

2016 was also a year of completion and delivery for Drax Group.

14,150

Jobs supported by Drax across the UK

"

IN 2016 WE PRODUCED 16% OF THE UK'S RENEWABLE ELECTRICITY FROM SUSTAINABLE WOOD PELLETS. WE STAND READY TO DO MORE.

In December the European Commission granted state aid approval for the Contract for Difference (CfD) to support the upgrade of our third generating unit at Drax Power Station to produce electricity from sustainable compressed wood pellets. That same month we completed the upgrade works and started producing 100% renewable power from the unit. This marked the final stage of our biomass transformation project which we have been implementing since 2012.

The transformation extends right across our supply chain. From the working forests of the Southern US to ports in the UK, it extends right through to the millions of homes and businesses across the UK that use the renewable power we produce.

In 2016 we produced 16% of the UK's renewable electricity from sustainable wood pellets. In total, we produce enough electricity to power Sheffield, Leeds, Liverpool and Manchester together. We stand ready to do more.

Through our retail business we supplied 7.5% of electricity required by UK businesses, whilst our pellet supply business produced 607,000 tonnes of compressed wood pellets.

According to a study published by Oxford Economics in 2016 (Draximpact.co.uk), Drax's total economic impact – including our supply chain and the wages our staff and suppliers' staff spend in the wider consumer economy was £1.2 billion, supporting 14,150 jobs across the UK.

MARKET OVERVIEW

The markets in which we operated were dominated by three major trends in 2016:

1. A tipping point for UK electricity

Firstly, the electricity market in Britain has now passed a tipping point. Until recently, intermittent generators such as wind and solar power have played a relatively small role in the electricity system. They are now playing an ever more significant role and the electricity system needs to adjust accordingly.

Britain now has 26GW of wind and solar installed – a six-fold increase over the last six years, and biomass has almost doubled its output since 2014 to over 14TWH.

Coal, which in the past has played a critical role in system stability and security contributed just 9.3% of Britain's electricity during 2016 – down from 42% in 2012.

Of course, these changes represent good news from the point of view of creating a low-carbon energy future. But they also create an increased need for flexible and responsive solutions to ensure stability and security of electricity supply for the UK's homes and businesses. This offers a major opportunity for Drax to provide more support services to the network in the areas of security of supply and system stability.

2. The growth of challenger brands in the retail market

Secondly, in the retail electricity marketplace, 2016 has seen a continued growth of challenger brands. It also saw the conclusion of a very important report from the Competition and Markets Authority (CMA) on the electricity market. This concluded that both the wholesale energy market and the business retail market are working well, with the exception of some concerns about micro-businesses. The CMA did conclude that concerns remain about the domestic retail market. Their recommendations focused on how consumers could get better deals.

3. Stress on wood pellet prices

Meanwhile the wood pellet market has suffered from a significant excess of supply over demand. This follows three warm winters in Europe where there is a large market for wood pellets for heating. Consequently, demand in this market has been depressed and many pellet producers have struggled to find customers for their output.

However, against this backdrop, there has been increased interest in biomass generation, particularly in the Netherlands and Japan with parallel policy developments expected to support more biomass generation. So, although the market has been severely stressed by excess supply, it is expected that demand for biomass will increase in future years.

PG.24 Marketplace review

POLITICAL AND ECONOMIC BACKGROUND

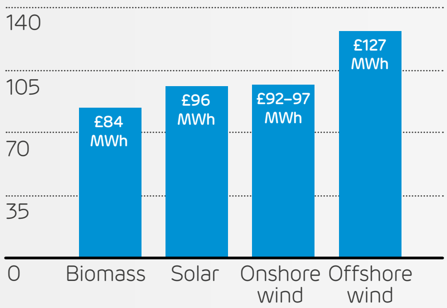
In 2016 we have been working against a background of significant political change in the UK. In general, the Brexit vote did not affect us because our electricity is used in UK homes and businesses. We purchase large quantities of fuel in foreign currency. However, we are well hedged against currency fluctuations for the next five years including the devaluation of Sterling in 2016.

2016 saw a reduction in our dependency on commodity-related earnings. A growing proportion of our earnings are now based on system support, pellet supply and retail sales, rather than pure commodity spread earnings from generating electricity. This will be even more evident in 2017, as a third of our biomass generation is supported under a CfD, which is not subject to movements in commodity prices.

SO WHICH TECHNOLOGIES ARE ACTUALLY THE MOST AFFORDABLE?

If biomass were allowed to compete in upcoming renewable auctions on a whole system cost basis, it would clearly be the cheapest technology.

CfD Strike Prices Including System Integration Costs



Prices based on lowest successful bids for each technology in the 2015 CfD auction. Biomass price based on conservative 15% discount on 2013 strike price and 15 year contract.

The UK Government continues to be clear that affordability of energy is a priority.

We commissioned research from Imperial College London and economic consultancy NERA to look at the affordability of biomass by factoring in whole system costs – essentially the hidden costs of power generation required to flex up and down to meet demand created by intermittent renewables. When these costs are built in biomass is seen to be the best value large scale renewable technology. If these new levels of support were to be reflected in the Government's planned energy auctions, the mix of generation that could win contracts is shown to save consumers up to £2.2 billion over a 15 year period.

SUSTAINABILITY

We apply robust and thorough sustainability standards in all of our biomass sourcing. Since 2008 we have used external experts to independently verify our compliance with these stringent standards. In 2015 the Sustainable Biomass Program (SBP) introduced the first sustainability certification system, including full life cycle analysis, for woody biomass. We are very pleased that in 2016 the SBP fully certified both our compressed wood pellet manufacturing plants.

Because sustainability is so central to our business, we are also delighted to report that carbon emissions from the generation of electricity at Drax Power Station fell by 53%(1) in 2016, partially driven by replacement of coal with biomass.

PG.36 Sustainability review

HEALTH AND SAFETY

The health and safety of all our employees and contractors is of paramount importance to Drax. The Group delivered a world-leading performance in 2016. Overall, this has been our best year since 2012. It is especially pleasing given that it was delivered against a backdrop of an intense schedule of planned maintenance on our generating units during the year which resulted in man hours worked being nearly five million across the Group.

Safety remains at the centre of our operational philosophy and we are continuing to work to improve our performance across the Group.

BUSINESS PERFORMANCE

Drax Biomass

2016 was a year characterised by flexible operations at Drax Biomass, curtailing production for a time to enable the Group to capture value in the distressed wood pellet spot market. Both our pellet plants are now working at full capacity and delivering pellets of good quality.

In 2016 we continued to work on optimising production from both pellet plants and identified the opportunity for making low cost, incremental capital investment which will increase the capacity of each of the facilities from 450,000 tonnes to 525,000 tonnes. We will make this investment in 2017 and deliver the increased capacity by the end of the year.

(1) See table 1 on pg. 42

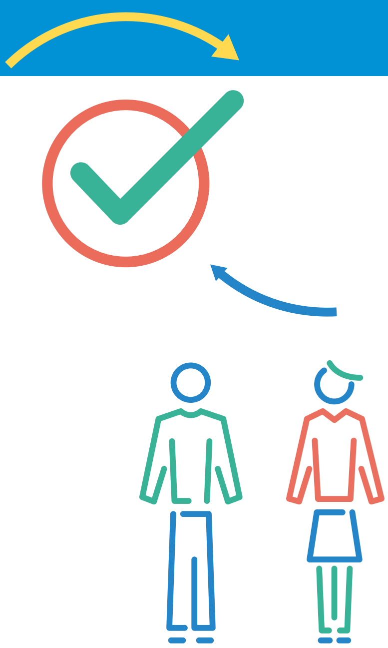
PG.28 Drax Biomass review

17%

Increased capacity at our pellet plants by the end of 2017

HEALTH AND SAFETY

The health, safety and welfare of employees continues to be the highest priority across the Group. Each business unit and corporate team has local arrangements in place, appropriate to the operating environment and hazards inherent in the various workplaces, to ensure that high standards are set and maintained.



Well established Safety Management Systems (SMS) are used to deliver safe places to work for all our teams. In Drax Power the SMS is certified to OHSAS 18001 and subject to regular compliance reviews, the last of which took place during 2016. In Drax Biomass the SMS is designed to be compatible with OHSAS 18001 and the United States certification ANSI Z10.

Safety performance is reported and reviewed regularly by local management teams, the Executive Committee and the Board. Each incident is comprehensively analysed and reviewed, lessons learnt are shared with employees and actions are taken to mitigate against future failures.

For the Group the Board received monthly reports which include Lost Time Injury Rates (LTIR), Total Recordable Injury Rates (TRIR) and numbers of RIDDORs (or US equivalent). The TRIR is included in the Group Scorecard (shown on page 98).

Performance on each KPI during the year was positive, with results better than targets. The results are shown in the table below.

	2016 Actual	2016 Target	2015 Actual
LTIR	0.02	0.10	0.05
TRIR	0.22	0.35	0.31
RIDDOR	4	6	2

LTIR is calculated by summing fatalities and lost time injuries per 100,000 hours worked.

TRIR is calculated by summing fatalities, lost time injuries and medical treatment injuries per 100,000 hours worked.

Drax Power

In 2016, 65% of our electricity was generated from sustainable compressed wood pellets.

Of the much smaller proportion of our electricity generated by coal, the vast majority was used to fill the gaps when additional capacity or flexibility was needed by the grid. All of our generating units at Drax are flexible, dispatchable, and responsive, making them ideal to adapt to the changing needs of the market, and to fill the gaps created by the increasing amount of intermittent renewable generation.

The future of our coal units remain uncertain. The Government published a consultation in November 2016 requesting views on whether conditions should be put in place requiring all coal power stations to close by 2025.

In 2016, Drax participated once again in the capacity market. While we are prohibited from doing this with our biomass units we did bid in two of our three coal units. Both units succeeded in securing a contract worth £13.6 million per unit per year for 2020/21. We elected not to bid for our third coal unit, as with the right conditions, we remain committed to upgrading further coal units to biomass. Had we bid in the capacity market, this would not have been possible in a timely manner.

PG.30 Drax Power review

Haven Power

In 2015, Haven achieved the scale of business which we were targeting for market access for renewable products and power.

The focus for 2016 has been to design a strategy that would deliver attractive levels of profitability at that scale. This strategy is focused on rebalancing our portfolio of sales to increase the number of small and medium-sized enterprise (SME) customers in our portfolio compared to those from large industrial and commercial (I&C) businesses.

PG.34 Haven Power review

With a new leadership team in place, Haven is now well placed to become a more nimble, agile business, embracing change and providing intelligent energy solutions for its customers.

Billington Bioenergy

For our wood pellet business Billington, 2016 was a year of uncertainty as the Government reviewed its policy for renewable heat across the UK. The new Renewable Heat Incentive tariff rates were finally confirmed in December, at a level that should support steady growth in biomass heating for both domestic properties and larger commercial scale plants.

Against this backdrop Billington continued to deliver a steady performance and has developed an attractive new strategy to grow the business at the scale and rate required to play a significant role in the Group.

OUR NEW STRATEGY

We announced the Group's new strategy in December 2016. It reflects our determination to continue playing a vital role in the way energy is generated, supplied and used as the UK moves to a low carbon future.

It is designed to help us deliver a stronger, more predictable, long-term financial performance for the Group along with greater diversification in the markets in which we operate.

In December we also made it clear how we would start delivering the strategy. We announced our proposed acquisition of business-to-business energy supplier Opus Energy along with that of a project to build four new rapid response Open Cycle Gas Turbines (OCGT) power stations.

The Opus acquisition was a major transaction and was subject to shareholder approval. The acquisition was approved by shareholders on 8 February 2017 and completed on the 10 February 2017.

Acquiring Opus is directly in line with our strategy of expanding our retail activities into the SME marketplace where it is already very successful as a challenger brand.

Opus has a well-established business as a dual fuel supplier, enabling us to supply gas as well as electricity to end users, which is critical to succeeding in the SME market.

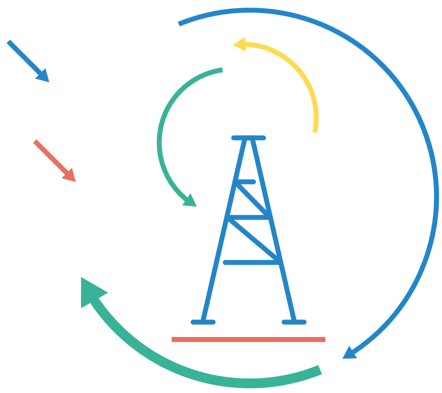
As the UK has now passed the tipping point where intermittent renewable generation plays a significant role in the electricity market, more rapid response power plants are required to keep the system stable.

This is exactly what the four 299MW OCGT plants we are planning to develop and build are designed to do. Two could be generating electricity as early as 2020/21, and the others by 2023/24. Each is capable of reaching full capacity in just 10 minutes – one third of the time taken by a conventional gas plant, enabling them to "fill gaps" whenever they might arise.

This capability for rapid response generation can enable Drax to play a vital supporting role in the UK's transition to secure low-carbon electricity which is cost-effective and reliable.

Our intention is only to go ahead with building these plants if we can secure an attractive capacity contract to provide the base revenues required.

Similarly, we have also announced our intention to expand our sustainable compressed wood pellet production operations to support self-supply of at least 20–30%. This will require a capacity of at least 2 million tonnes per annum, double our current capacity. However, we will only move forward with this expansion if we identify attractive opportunities, including the potential acquisition of financially distressed pellet plants in the US.



STRATEGY ENABLERS

The first key enabler is our new people strategy. We are nothing without our people, and our greatest challenge will be further developing the excellence, talent and skill sets of the teams to ensure the successful delivery of our new strategy across all our businesses, including our recent acquisitions. That is the driving force behind our new people strategy, which is outlined on page 45 of this report.

The second key enabler is our new IT strategy which will deliver a step-change in the way we work across the Group. It will not only transform our day to day ways of working, making us more efficient, but also improve our analytic capacity and create a digital capability that will put data at the heart of all our work.

OUTLOOK

Our focus in 2017 is on delivering the new strategy whilst continuing to deliver excellence across the base business.

For Retail the year ahead will see Haven and Opus working closely together to deliver a compelling offer to the UK's businesses. The two businesses complement each other perfectly, and two challenger brands will between them offer expertise and experience in supplying gas and electricity to both small and medium-sized enterprises (SMEs) and industrial and commercial customers (I&Cs).

There is a clear focus on embedding Opus into the Group. This is based on recognising the fact that the key to our future success together will be continuing to enable the Opus team to develop their skills and share their best practice across the Drax family.

For Drax Biomass the focus will be on quality and stability for existing capacity, low cost expansion at existing plants and, where available, targeting low cost acquisition of operating pellet plants and identifying possible opportunities to supply compressed wood pellets to new markets.

In our Generation business we will continue to deliver renewable electricity that is reliable and responsive through our biomass units. With the right conditions, we will begin conversion of three more units to run on compressed wood pellets. We see our coal units as playing an important role in system stability and capacity support.

And we will work on the development of our four rapid-response OCGT plants with the firm intention of committing to further investment as soon as the UK capacity market clears at a price that provides a robust underpinning for such investment.

Having taken the first steps in developing our new strategy, we will continue to look for opportunities to further enhance and build on it, ensuring we play an even greater role in delivering the secure and stable supply of low-carbon, reliable and affordable electricity the UK needs.

Dorothy Thompson
Chief Executive, Drax Group

2017 PRIORITIES

GENERATION
OCGT DEVELOPMENTS
- Capacity and flexibility support
- Using core competencies
- New long-term generation earnings
- Market opportunities in peak price periods
- Diversified generation mix
- Attractive financial returns

BIOMASS FUEL AND SUPPLY
PELLET SUPPLY OPPORTUNITIES
- Targeting 20–30% self-supply
- Evaluating opportunities to acquire distressed assets
- Attractive financial returns

RETAIL
OPUS ENERGY
- Acceleration of retail strategy
- Platform for growth
- Compatible and complementary to existing retail business
- Advances transition to broader, higher quality long-term earnings
- Synergy potential
- Attractive financial returns

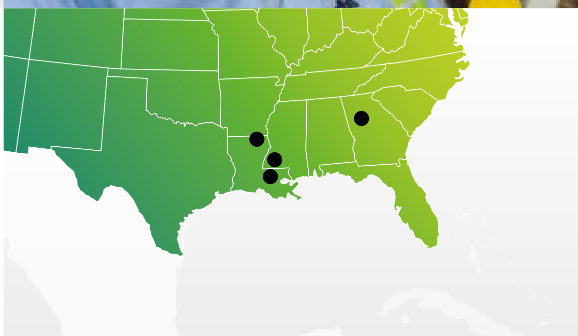
SMART SOURCING

Reliable, renewable and affordable electricity begins with sustainable sourcing. Drax's biomass supply chain reaches deep into the expansive working forests of the Southern United States.

These forests provide an abundant supply of low-grade wood, including thinnings and harvesting residues that have previously been underutilised by the forest products industry. We transform this material into high-quality, sustainable compressed wood pellets that are helping the UK to decarbonise.

drax biomass

Since the early 1950s, forest stocks in the US South have increased by 107% (5 billion cubic metres) within a stable total forested area (99 million ha in 2012). This increase is driven by improved forest management and a robust forest products industry, encouraging landowners to reinvest in their working forests. These landowners provide Drax with a ready supply of sustainably grown and harvested wood that we transform into high-quality compressed pellets. We bolster the market for low-grade and underutilised wood in areas that have suffered from a decline in the pulp and paper industry.



OUR ACHIEVEMENTS:

- Our pellet manufacturing facilities in Mississippi and Louisiana achieved significant operational gains this year, increasing total production by 118% to 607,000 tonnes in 2016, and achieving record daily and monthly production levels.
- Our storage and loading facility dispatched 11 ships to the UK, including our first-ever Panamax vessel carrying over 61,000 tonnes. Bulk shipping cost-effectively reduces transportation-related carbon emissions.
- Both pellet facilities achieved certification under the Sustainable Biomass Program (SBP) – the foremost industry standard demonstrating that biomass is legally and sustainability sourced.

OUR AIMS AND OBJECTIVES:

- We aim to increase pellet manufacturing capacity to at least 1,050,000 tonnes per year through engineering improvements at our existing facilities and investment in new facilities.
- We aim to supply Drax Power Station with 20–30% of annual demand for wood pellets.
- We aim to provide new customers in other regions with a dependable supply of high-quality, sustainable wood pellets.

LOCATIONS

Drax Biomass is headquartered in Atlanta, Georgia, and operates two facilities in Louisiana and Mississippi. Morehouse BioEnergy near Bastrop, Louisiana and Amite BioEnergy in Gloster, Mississippi, produce a steady supply of high-quality wood pellets, shipped to the UK through our Baton Rouge transit storage and loading facility in Port Allen, Louisiana.

4

key sites in the US

AN INNOVATIVE, TECHNOLOGY-LED APPROACH

Drax Biomass sources raw materials from working forests that supply a diverse range of wood-based manufacturing. The largest, most valuable stems – sawlogs – are typically sold to sawmills for use in the construction industry.

We take the least valuable wood, including small-diameter thinnings removed early in a working forest's life cycle, to improve productivity of the remaining trees. We also use tops, low-grade wood and other by-products from harvesting operations, along with wood chips, shavings and sawdust from other wood-based manufacturing facilities.

GROWING VALUE AND FORESTS

We help revitalise communities which have lost jobs in traditional industries, including pulp and paper. We support local landowners through steady and dependable demand for their low-grade wood. Without such a market, much of this low-grade timber might go unused. Other material, such as thinnings, may not be harvested at all, and reduce a stand's health, productivity and capacity to produce valuable sawtimber. This would lead to less income for landowners and less incentive to reinvest in, or retain, their working forests. Strong markets are critical to long-term forest growth, a relationship that is clear to see in the US South where harvests increased by over 46% during the same period in which total inventory grew by 107%.

LESS MOISTURE LEADS TO LESS EMISSIONS IN TRANSPORT

Water makes up roughly 50% of a tree's weight, so reducing the moisture level makes our transportation process more efficient. The pellets we produce are very dense, so we can squeeze more mass – and energy – into a rail car, lorry or cargo vessel, avoiding unnecessary carbon dioxide emissions.

A STRATEGIC HUB

Our storage and loading facility at the Port of Greater Baton Rouge is a strategic hub for Drax Biomass and our customers. Our two 40,000 tonne storage domes can handle pellets from our own mills, from approved third-party suppliers as well as from new capacity that comes online through our growth strategy.

Pellets are unloaded and transferred to the domes through a system of conveyors and transport towers, then moved to a ship loader to finish the process. This can handle more than 15,000 tonnes of pellets per day, so we can load a cargo vessel in as little as three days.

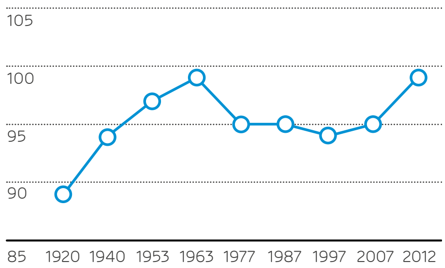
By locating our storage and loading facility at a deepwater port, Drax Biomass can use larger cargo vessels to minimise our transportation-related carbon dioxide emissions. In December 2016, we shipped our first-ever Panamax vessel loaded with over 61,000 tonnes of pellets.

81M

dry tonnes of surplus wood in the US South. The forests we work with in the US have 206 million dry tonnes of annual growth set alongside 126 million dry tonnes harvested, resulting in a significant surplus availability

US South Forest Area

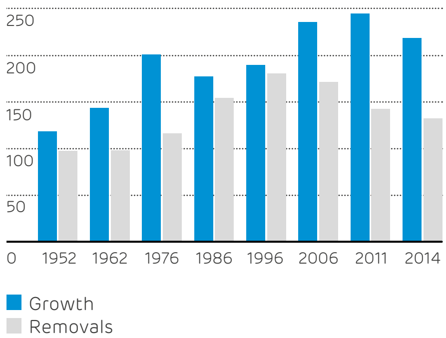
Area Ha (million)



Source: USDA Forest Service

US South, growth vs removals

Million tonnes



Note:
Original data converted to dry tonnes using an assumed moisture content of 50%.

Source: USDA Forest Service

FOR MORE SUSTAINABILITY STORIES VISIT DRAX.COM

SUSTAINABILITY

PROTECTING NATURAL TREASURES

Drax Biomass is committed to continually reviewing and improving our sourcing practices. This includes working with local stakeholders to identify areas of unique ecological value, and to implement additional protections to ensure our operations don't adversely impact those areas.

In 2016, for example, we unveiled a collaboration with the Atchafalaya Basinkeeper, a local environmental organisation dedicated to protecting the Atchafalaya Basin – a vast system of bayous and forested wetlands in South-Central Louisiana that is home to a diverse array of animals, birds and other wildlife. This collaboration centred on a set of sourcing commitments designed to protect the Basin and other similarly important ecosystems while allowing the wood pellet industry to operate.

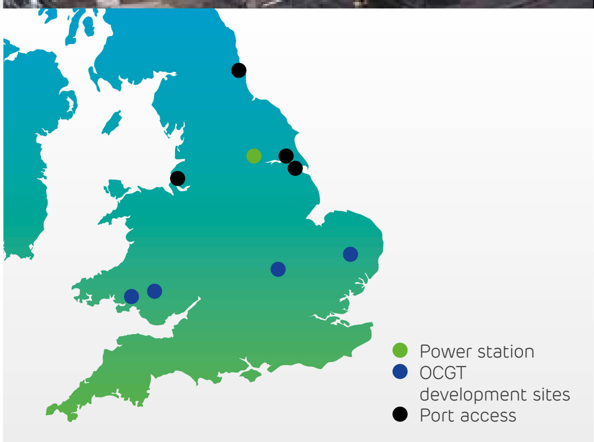
> "WE WORK WITH LOCAL STAKEHOLDERS TO ENSURE OUR OPERATIONS DON'T ADVERSELY IMPACT IMPORTANT AREAS.

SMART GENERATION

Drax Power Station generates 7% of the UK's electricity. We are the largest power station in the UK, and also the UK's largest single site renewable generator, producing 16% of the country's renewable electricity.

We have successfully completed our strategy to upgrade three of our generating units to be powered by compressed wood pellets rather than coal and received our Contract for Difference (CfD). We stand ready to do more. Our new strategy has set out how we intend to complement our current generation capacity with new rapid response gas projects. We will continue to produce reliable, flexible and lower-carbon electricity and help secure stability of supply for the whole country.

drax power



Drax Power Station is located in Selby, North Yorkshire and is connected directly to the national distribution grid, and to the rail network.

The power station consists of six generating units. Three of these run on compressed wood pellets and three use coal. Our four planned rapid response gas generating sites in England and Wales will each have the capacity to produce 299MW of electricity.

7%

of the UK's electricity is generated by our six generating units

Drax Power plays a key role in ensuring the security of the UK's energy supply, now and in the future. We currently generate 7% of the UK's total electricity at Drax Power Station. In 2016, 65% of this came from biomass. We plan to generate electricity using Open Cycle Gas Turbines (OCGTs) at four new sites in England and Wales.

OUR ACHIEVEMENTS

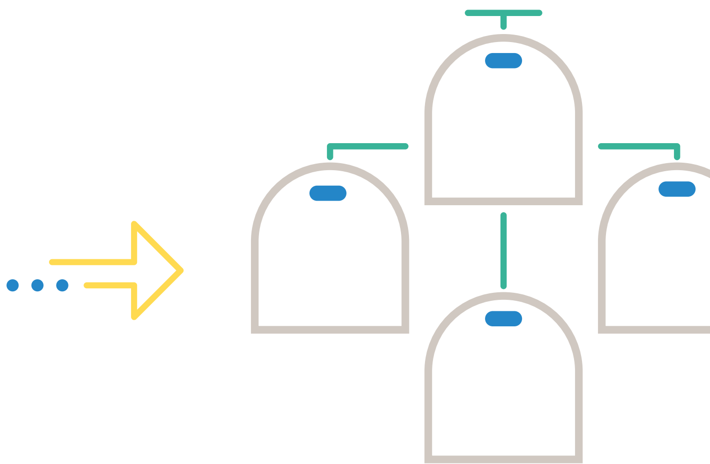
- We have developed a whole new technology to upgrade three of our generating units to be powered by compressed wood pellets and received clearance for our CfD.
- 65% of our production was generated from biomass in 2016.
- We have renewed contracts to supply ancillary services systems support.
- We have reduced NOx emissions by 53% compared with 2015 and complied with the Industrial Emissions Directive.

OUR AIMS AND OBJECTIVES

- We will diversify our energy generation, adding the potential for more than 1GW of rapid-response OCGT generation at four sites in England and Wales.
- We will seek further efficiencies at the power station and throughout the supply chain in order to improve margins.
- We will reduce maintenance costs by £10 million this year during our planned outage programme on one of our coal units.
- We will use our unique flexibility and reliability to provide more system support services to National Grid.
- We stand ready to upgrade more of our generating units to be powered by compressed wood pellets.

WORLD-LEADING BIOMASS TECHNOLOGY

Drax Power Station is home to some of the UK's most advanced generating technology. Much was developed by our in-house engineering team in order to upgrade three of the generating units, enabling them to be powered with compressed wood pellets. We continue to lead the way in reliable, renewable generation at significant scale.



GENERATION UPGRADE STRATEGY DELIVERED

2016 saw the full conversion of the third generating unit to be powered by sustainable biomass pellets rather than coal. This means half the power station has now been upgraded to produce renewable electricity. It also saw the European Commission clear our CfD under rules for state aid, meaning the original upgrade strategy is now complete. Our team of engineers and those of the many partners who helped us deliver this strategy can rightly be proud of what is an enormous achievement.

We are now the UK's largest single site renewable generator. We remain convinced that upgrading existing coal-fired plant to be powered by compressed wood pellets is the most effective, efficient way to remove coal from the system altogether, and that it is the approach that will come at the lowest cost to the consumer and the taxpayer. In 2016 we commissioned new research from Imperial College London and economic consultancy NERA to look at the comparative affordability of biomass. The research assessed renewable technologies on a whole system costs basis and found biomass to be the most cost-effective large scale option.

At Drax we stand ready to upgrade more of our capacity.

CLEANER ELECTRICITY

65% of our output in 2016 was generated using sustainable biomass pellets, making our electricity this year the cleanest it has ever been. As well as reducing carbon emissions by at least 80% when compared with coal, this electricity was also generated with 53% less NOx emissions than in the previous year thanks to a major investment in new technology at the plant.

SEEKING FURTHER EFFICIENCIES

Now that we have proved the viability of large-scale upgrades to biomass, our challenge is to improve the efficiency of the entire biomass supply chain, particularly following the recent movements in the exchange rate between the US dollar and the pound sterling. We are strongly hedged against further depreciation in sterling until 2021, but greater efficiency will help us even more.

SUCCEEDING IN CHALLENGING CONDITIONS

These successes have been achieved against a background of very challenging conditions at the power station. Five out of six generating units have required significant work, and employees and contractors have carried out over four and a half million hours of work on site.

Some of this work has been enormously demanding. Drax may well be the only power station to have replaced the entire main steam pipework system on one of its boilers within the lifetime of the plant itself.

There have also been some unplanned events, but we have successfully managed our biomass supply chain and adjusted to meet these challenges.

19.6TWH

Generated during 2016

6.6M

Tonnes of biomass used

2.7M

Tonnes of coal used

"

WE HAVE NEARLY HALVED OUR CARBON EMISSIONS, MAKING US EUROPE'S SINGLE LARGEST DECARBONISATION PROJECT.

TECHNOLOGY

RAPID RESPONSE SYSTEM SUPPORT

In December 2016, Drax Group acquired four sites where we plan to build new state-of-the-art flexible power stations. The sites are near Merthyr Tydfil and Swansea in South Wales, and in Suffolk and Bedfordshire in England.

Two of the OCGT plants could be generating electricity by 2020/21 and a further two in 2023/24. The Open Cycle Gas Turbine technology will mean these power stations reach full capacity just ten minutes after being started up. This provides vital flexibility to help provide system support. Flexible, rapid-response power like this will help fill the gaps caused by system stress. It will help support the increasing amount of intermittent renewables such as solar and wind. It will also help to accelerate the rate coal comes off the system.

10 MINUTES

The four OCGTs can reach full capacity in 10 minutes

FOR MORE TECHNOLOGY STORIES VISIT DRAX.COM

THE FUTURE OF COAL GENERATION AT DRAX

We will continue to invest in coal generation at the power station, but on a case-by-case basis depending on the return on investment and clearly we do this against the background of the Government's aim to remove coal from the system by 2025. We have deferred a planned outage on unit 6. We see limited running on this unit over the summer months because we have two other coal units to provide system support and therefore deferring the outage should not impact its operation.

SYSTEM SUPPORT SERVICES

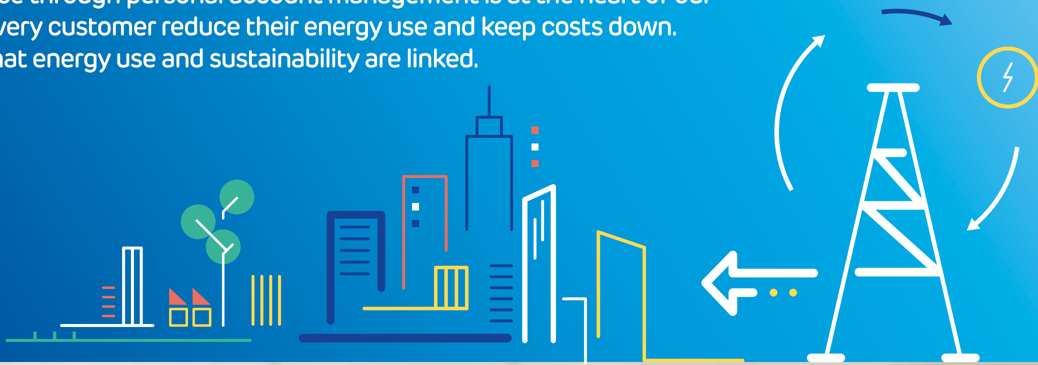
Drax Power has identified a growing need for system support services and is very pleased to have signed ancillary services contracts, at the power station. In 2016 the flexibility and responsiveness of our coal-fired units was used in the energy market, by running summer overnights to provide system support. Our coal units have also provided much-needed services in the winter market when capacity is tighter. Our policy of not selling forward on the power from our coal units and leaving it free to be sold in real time has proven to be a very successful strategy.

SMART SUPPLY

Haven Power gives businesses the option to choose electricity that is both renewable and reliable, unlike that from intermittent energy sources such as wind or solar.

The addition of Opus Energy to the Drax Group strengthens our retail offer, enabling more businesses to access the type of energy they want.

Outstanding customer service through personal account management is at the heart of our business. We offer to help every customer reduce their energy use and keep costs down. We help them understand that energy use and sustainability are linked.



havenpower

72%

of SMEs want their energy supplier to be more committed to renewable energy[1]

Haven Power gives Drax Group a credit-efficient route to market for the reliable, renewable power it generates, while also enabling businesses across the UK to reduce their carbon emissions and keep their energy costs down.

OUR ACHIEVEMENTS

- We have grown to a size where we are well set to develop our profitability and improve gross margin further.
- We are focusing on helping more customers than ever to reduce their energy consumption, including encouraging industrial and commercial customers to use less when demand – and costs – are high.
- The high number of renewals means our UK-based contact centres are delivering the excellent customer service that we promise.
- We have integrated many of the back-office operations of Billington Bioenergy into Haven Power.

OUR AIMS AND OBJECTIVES

- We aim to improve our profitability.
- We aim to build relationships with customers who have told us they are looking for reliable, renewable electricity, and give advice to help them to reduce energy use and costs.
- We aim to help more businesses understand and reduce their energy. We will rollout smart meters and use the data they produce to empower us to do more.
- We aim to diversify and give more customers an energy supplier that can satisfy their needs and preferences, simply, efficiently and reliably.

OPUS energy

- With the introduction of Opus Energy to the Drax Group, we are even better placed to achieve all our aims. It enables us to build a profitable challenger retail offering, providing businesses with everything they need.
- Opus Energy has 265,000 customer meters, making it the sixth biggest supplier to UK businesses and, because of this, we will soon be in a position to give many more small and medium-sized enterprises (SMEs) access to the type of energy they want, along with higher levels of choice, service and value.
- Opus will allow us to accelerate our retail strategy and give us a platform for profitable growth.

(1) Haven Power research report into SMEs.

"DISRUPTIVE ENERGY"

Jonathan Kini joined Haven Power in January 2016. In April 2016 he was named CEO, and in September 2016 he joined the Drax Executive Committee. Jonathan's experience at Virgin Mobile has given him great insight into the ways that challenger brands can disrupt the marketplace. As Jonathan says: "I'm keen to shake this market up. We need to improve the trust equation radically. We're committed to making it easier for every business in the UK to find the reliable, renewable electricity they want, to go green, and to save money."

"

WE'RE COMMITTED TO MAKING IT EASIER FOR EVERY BUSINESS IN THE UK TO FIND THE RELIABLE, RENEWABLE ELECTRICITY THEY WANT, TO GO GREEN, AND TO SAVE MONEY.

Jonathan Kini
Chief Executive Officer,
Drax Retail

HELPING CUSTOMERS

The majority of Haven Power sales volumes are with larger industrial and commercial customers. While we continue to develop this market, Opus Energy now allows Drax to have an increased focus on the UK's 5.4 million SMEs.

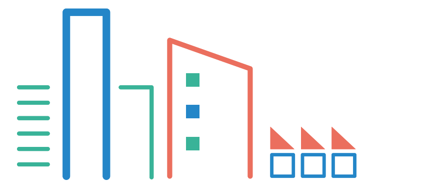
Our recent research(1) shows that a significant number of SMEs are keen to switch to renewable energy. However, in many cases their staff are so busy that time is at a premium – they need a partner who can make it easy to switch. Our excellent customer service means it is easy to switch, and because our renewable electricity does not rely on the sun or the wind, we are able to offer a truly reliable supply.

6%

year-on-year retail power sales volume growth

14.6TWH

electricity sales



MANCHESTER AIRPORT GROUP (MAG)

MAG has been a Haven Power customer since 2011.

"Haven Power have consistently provided excellent customer service and a reliable, renewable product. When we originally made the switch in suppliers five years ago our dedicated team at Haven ensured the process was extremely smooth and efficient, which set the mark for the service that has followed."

Tim Hooper
Head of Group Procurement and Contracts, Manchester Airport Group

THAMES WATER

Thames Water is one of our larger customers at Haven Power.

"The option to be supplied with renewable power is very important to Thames Water and we were impressed by Haven Power's offering in this area. Since joining Haven we have received excellent levels of customer service from our dedicated Account and Service Managers who ensured an easy transition and consistently provide an efficient and professional service."

Angus Berry
Head of Energy and Carbon, Thames Water

(1) You can download a copy of our research report into SMEs at http://havenpower.com/sme-report

CARBON-SAVING TECHNOLOGY

Haven is committed to helping customers understand the link between energy use and sustainability. We welcome the Government's decision to roll out smart meters to all small business customers by the end of 2020.

The real-time information that smart meters provide will give Haven valuable information about how customers are using energy. This will help us develop new products that can help them optimise their use and reduce their carbon footprint.

OPUS energy

STRONGER TOGETHER: HAVEN POWER AND OPUS ENERGY

The majority of Haven Power's contracts are in the large industrial and commercial market, although we still supply 2TWH to SME customers. Opus Energy has significant expertise and is a strong presence in this sector. It is the sixth largest business power supplier by meters in the UK, delivering nearly 5TWH of electricity a year to its customers, supported by a team of 800 employees and working from three locations across the UK.

Opus Energy brings with it some additional services. It is a substantial gas supplier and has the capability to provide a route-to-market for any renewable electricity produced by SME customers that they do not need or cannot use themselves.

The two businesses complement each other and together are best placed to deliver smart solutions to businesses in the UK calling for more renewable and lower carbon energy.

The acquisition at Opus Energy was completed on 10 February 2017.

BILLINGTON bioenergy

BILLINGTON BIOENERGY

Established seven years ago, Billington Bioenergy helps homes and businesses across the UK to heat their properties and reduce their carbon emissions through biomass heating.

We provide certified ENplusA1[1] wood pellets for biomass heating systems. With thousands of regular business and domestic customers, we are now one of the UK's leading biomass pellet suppliers.

BILLINGTON BIOENERGY'S ACHIEVEMENTS

- Robust supply chain providing a strategic mix of UK and European ENplus A1 wood pellets, certified to the highest European standard.
- Many back-office operations now integrated with Haven Power for greater efficiency.
- Extended national depot infrastructure integrated with existing Drax access to port facilities.
- New e-commerce website with online bagged sales facility.

AIMS AND OBJECTIVES

- Drive further sales growth to consolidate leadership position in domestic and business pellet supply.
- Develop software to enhance our market-leading customer service.
- Implement industry-leading best practice health and safety policy and procedures.

(1) EnplusA1 is a European-wide quality standard incorporating specification ISO17225-2.

32,000 TONNES

2016 wood pellet sales volumes

SUSTAINABILITY

THE NATIONAL TRUST

Billington Bioenergy has a national procurement contract with the National Trust, one of the UK's largest conservation charities. For the past two years, Billington have provided sustainable biomass pellets to the National Trust's property at Nostell Priory.

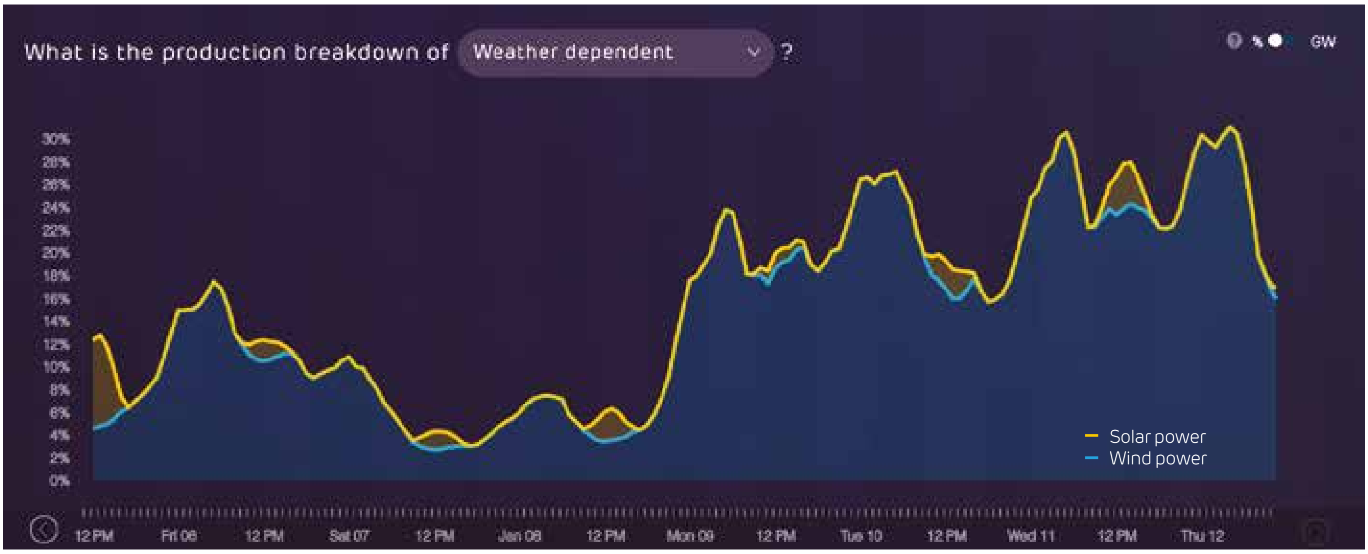
> "THE BIG FACTOR WAS THE ENVIRONMENTAL BENEFIT – THAT'S THE KEY THING FOR US.

Tracy Sykes
Facilities Manager at Nostell Priory

OUR MARKETPLACE

The last 12 months have seen an acceleration of the changes that have affected the UK electricity market over the last few years. The overall picture was one of rising low-carbon generation, falling coal use, falling emissions and increasing grid volatility.

All of these trends have provided challenges to Drax's business and required skill and expertise to manage.



electricinsights.co.uk

50%

More than 50% of total electricity generated in the third quarter of 2016 was low carbon

Over the course of the year, 3.2 GW of new wind and solar farms came online, and in the third quarter the share of low-carbon power from nuclear, biomass, hydro, solar and French imports passed 50% for the first time ever.

Coal capacity was lost due to a combination of factors, particularly tougher clean air legislation and diminishing economic returns. It fell to its lowest level ever, producing just 9% of the country's electricity. Four years ago, coal was still producing 42% of the UK's power.

INCREASED VOLATILITY

The rise in intermittent renewables is changing the way the entire electricity system works, with a move away from dispatchable fossil-fuelled electricity to a greater proportion of weather-dependent renewables. This is challenging for the UK electricity system. It is also an opportunity for Drax.

It will be some years until significant new capacity is added to the system.

A number of small-scale gas and diesel plants are expected to come online but the only large-scale plant due to begin generating in 2018 (Trafford) has now defaulted on its capacity agreement. This means that in reality, the earliest date at which new large-scale flexible plant will actually come online is now 2021.

The planned expansion of intermittent generating capacity continues, with 8.5 GW planned to come online between 2017 and 2020, which means that volatility will remain high for the foreseeable future.

42%

of electricity in the UK produced from coal in 2012

9%

of electricity in the UK produced from coal in 2016

ANCILLARY SERVICES

Thanks to increased renewable generation, carbon dioxide emissions associated with electricity are being reduced, as gas and coal-fired plants are producing less of the UK's power needs.

However, in order for the entire system to run reliably, there are a number of requirements that can only be met by flexible generation plant.

This results in National Grid requiring certain plants to provide services including: frequency response, reactive power, the capacity for headroom or footroom, black start and other ancillary services.

Demand for these services has gone up and the cost of providing them from conventional plants has become more expensive (this is because the plants have to be kept running in order to be able to provide the ancillary services required). Consequently, prices for these services are rising and we expect this to continue.

We see an opportunity to provide more ancillary services from Drax Power Station in the coming year.

Drax's plan to add generating capacity powered by rapid response Open Cycle Gas Turbines (OCGTs) will fit the increasing need for headroom. In fact OCGTs are ideally suited to this, as they can reach full running capacity within 10 minutes of being turned on (this compares with 90 minutes for a Combined Cycle Gas Turbine (CCGT) power station).

BIOMASS CONVERSION

With the receipt of our Contract for Difference (CfD) and the completion of the upgrade of our third generating unit to be powered by sustainable compressed wood pellets rather than coal, the first stage of our biomass conversion strategy is complete.

Upgrading generating units to be powered by sustainable compressed wood pellets as developed at Drax Power Station remains the only flexible and reliable source of large-scale low carbon power.

Another advantage of biomass upgrades of this kind is the fact that they are capable of providing many of the ancillary services discussed above while also producing low-carbon energy at the same time.

This means that flexible biomass-fuelled generation like that at Drax can replace flexible fossil plants that would otherwise still be needed to provide ancillary services to the Grid if the majority of electricity is coming from intermittent sources.

One example of this is footroom – the ability to turn down the electricity supply on demand – which requires constant running from OCGTs or other fossil fuel plant, making it more challenging to meet targets for the reduction of carbon dioxide emissions.

Lower system integration costs compared to other renewables make biomass conversion the lowest-cost way to achieve decarbonisation in electricity generation. A 2016 report from Imperial College London and economic consultancy NERA found that on a whole system costs basis, biomass is the most affordable large scale renewable. If this was applied to the Government's planned CfD auctions biomass conversions are shown to be £84 per MWh compared with offshore wind at £127 per MWh.

HEAT SECTOR

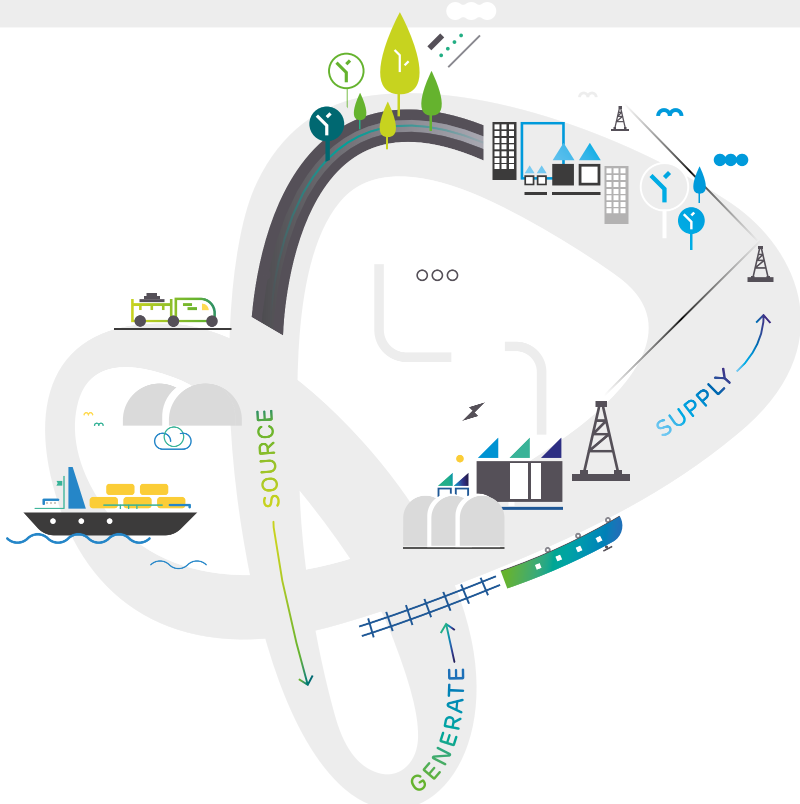
While biomass systems have achieved significant volumes of deployment in the domestic and non-domestic sectors in recent years under the Renewable Heat Incentive (RHI), there were comparatively modest levels of activity in the market in 2016. This was due to a combination of uncertainty over the future of the RHI following proposals published by Government to reform the scheme, and historically low oil prices.

However the outlook for the sector became more positive as the year drew to a close. The Government announced its final reforms to the RHI, proposing an uplift to support rates for domestic biomass systems and bringing all biomass systems under a single tariff under the non-domestic regime. This will provide installers and customers with greater certainty over the future of the support scheme and should stimulate renewed activity in the marketplace over the coming months.

Meanwhile, the price of oil has gradually increased, making the proposition of switching to a sustainable, renewable alternative more attractive to existing oil heating as well as off-grid gas users.

OUR BUSINESS MODEL

Our business model is based on an integrated value chain.



drax biomass

SMART SOURCING

RAW MATERIALS
Biomass fibre is sourced from working forests with a surplus of available material

Coal is purchased from global suppliers and often blended with reclaimed materials **PG.41**

PROCESSING
Wood pellet manufacturing facilities produce biomass fuel, including our own sites in the Southern US **PG.28**

LOGISTICS
Biomass and coal fuels are transported efficiently in large volumes, using sea and rail routes

Facilities at UK ports (Liverpool, Hull, Tyne and Immingham) manage imported fuels

900,000

Our two pellet processing plants in the US can produce 900,000 metric tonnes of compressed wood pellets every year

drax power

SMART GENERATION

FUEL STORAGE
At the power station biomass wood pellets are stored in climate-controlled domes, each with a 75,000t capacity

POWER GENERATION
Six generating units each have an output capacity of 645 MWh. Three units use biomass fuel and three use coal

Generation of renewable power delivers earnings from ROCs and a CfD **PG.30**

TRADING
Trading of power and ROCs takes place in wholesale markets

Power sales are hedged where liquid markets exist, minimising price risks

16%

In 2016, Drax Power produced 16% of the UK's total renewable electricity. We have the flexibility to help meet electricity demand when intermittent renewables such as solar or wind power cannot generate

haven power

SMART SUPPLY

SALES
Sales teams in each business focus on market segments, negotiating annual and multi-year contracts **PG.34**

DISTRIBUTION
Multiple virtual and physical routes exist for customers across all business sectors to access a range of power and heat market products

CUSTOMER SERVICE
Excellent customer service is standard for each business

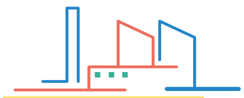
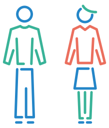
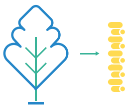
Dedicated teams ensure high-quality advice and support is available, minimising complaints and quickly resolving issues **PG.12**

14.6TWH

Haven Power increased 2016 power sales from 13.8TWH in 2015 to 14.6TWH in 2016

GENERATING VALUE FROM OUR RESOURCES

Careful use of our resources, also known as capitals, allows us to create value for our stakeholders.

	USING RESOURCES	VALUE CREATED	MORE INFO
MANUFACTURING 	We deploy targeted investment to deliver high-quality manufacturing capabilities Output and efficiency are key targets, built on high health and safety standards	**12.7TWH** biomass-fired electricity **607,000** wood pellets produced	PG.31 PG.29
INTELLECTUAL 	We are experts and world leaders in deployment of biomass technology We offer "intelligent sustainability" to our retail customers Innovation is key to business development	Biomass generation represents **65%** of total generation	PG.33
HUMAN 	Excellent health and safety underpins everything we do Our people provide a wide range of knowledge and skills Our values (Honest, Energised, Achieving, Together) guide the way we work	**Only 4** reportable accidents **1,488** jobs worldwide	PG.21 PG.44
FINANCIAL 	We have good access to efficient debt, foreign exchange and trading facilities Bank facilities provide cash for working capital and investment Profit is generated to allow dividends to be paid to shareholders	Stable credit rating **BB RANGE**	PG.53
NATURAL 	We only source biomass fibre from working forests, where surplus stock is available Our biomass transformation programme has allowed us to shift away from coal to lower-carbon electricity generation Reducing our carbon output is central to our strategy	Biomass power generates at least **80%** less carbon than coal **100%** renewable power available to retail customers	PG.40
SOCIAL 	Each business has strong links to its local communities and we focus our charitable support on the areas where we operate We welcome visitors and our people volunteer in local communities	**16,428** Drax Visitor Centre visits **£125,233** donated to local charities in 2016	PG.49

draxbiomass

Pete Madden
President and Chief Executive
Drax Biomass

Drax Biomass helps Drax Group to deliver a better future by changing the way energy is generated. We manufacture and supply high-quality wood pellets sourced from sustainably managed working forests across the US South.

INTRODUCTION

Our pellets provide electric utilities with a renewable, low-carbon alternative fuel source – one that can be safely and efficiently delivered through our global supply chain. Our manufacturing operations also promote forest health by incentivising local landowners to actively manage and reinvest in their forests.

MARKET CONTEXT

2016 was a challenging year for the wood pellet industry. Global manufacturing capacity outpaced demand due to policy uncertainties, project delays and unseasonably warm winters in high-demand regions. This supply/demand imbalance placed downward pressure on pellet prices, disproportionately impacting those suppliers without long-term contracted demand. Depressed spot market pricing caused some pellet projects to be delayed or cancelled, which will help correct the supply/demand imbalance in the near-term.

Drax Biomass remained in a strong position through 2016 as a result of intra-Group sales to Drax Power under an arm's-length commercial agreement. We also sought to improve our cost profile through productivity gains, carefully managed raw fibre costs and increased asset utilisation.

OPERATIONAL REVIEW

Drax Biomass achieved several important operational milestones in 2016. Our Amite BioEnergy and Morehouse BioEnergy facilities saw significant production gains over 2015, with each achieving both daily and monthly record production levels several times over the course of the year. We have clearly demonstrated our ability to produce quality pellets at nameplate capacity. Our Baton Rouge transit port facility also achieved a major milestone in December, when we successfully dispatched our first Panamax class vessel – the *MV Jawor*. With a cargo of 61,461 tonnes, the *MV Jawor* is the largest-ever shipment of pellets.

Drax Biomass produced a total of 606,787 tonnes of pellets in 2016, representing just over 67% of nameplate capacity. We managed our production during the year to allow Drax Power to purchase pellets in the spot market at distressed prices. This was a clear example of one of the benefits of self supply.

FINANCIAL RESULTS

Drax Biomass 2016 financial results were driven by the volume of pellets sold to Drax Power Station under our commercial agreement. Sales of pellets in the year ending 31 December 2016 totalled $99.6 million, an increase of nearly 130% over 2015 sales revenue.

Cost of sales also increased in 2016 commensurate with our higher production volumes. Raw fibre procurement comprised the largest share of these costs, and this continues to be an important area of focus for the business. We successfully controlled these costs through a combination of measures, including improved forecasting of utilisation and increased purchases of more cost-effective feedstocks such as sawmill residuals.

The EBITDA loss for the year reduced to £6.3 million (2015: £14.8 million).

DRAX BIOMASS FINANCIAL PERFORMANCE

	2016 £m	2015 £m
Revenue	73.6	28.4
Cost of sales	(55.5)	(27.4)
Gross profit	18.1	1.0
Operating costs	(24.4)	(15.8)
EBITDA	(6.3)	(14.8)

FOR MORE SUSTAINABILITY STORIES VISIT DRAX.COM

SUSTAINABILITY

HOW TO MAKE A COMPRESSED WOOD PELLET

- Low-grade roundwood is delivered to the woodyard
- Roundwood is processed through a drum debarker and the bark is diverted for fuel use
- Debarked wood is chipped and stored on a woodchip pile
- Chips are recovered and screened for quality
- Screened chips are processed through a drum dryer to reduce moisture content
- Dried chips are pulverised into fibre in hammermills
- Fibre is extruded under pressure through metal dies to form compressed pellets
- Pellets are cooled before loading into railcars or trailers

KEY PERFORMANCE INDICATORS

607,000

Tonnes of pellets produced

558,000

Tonnes shipped

LOOKING AHEAD

Drax Biomass is optimistic about the future, and we are positioned for significant growth in 2017. We intend to execute several capital projects to increase our production capacity at both manufacturing facilities. In line with our strategy, we are also pursuing the acquisition of several third-party facilities to increase our asset portfolio and geographic reach. These measures will enable Drax Biomass to increase our share of Drax Power Station's pellet demand and successfully compete for supply contracts in new biomass markets. Finally, we will also generate additional revenue through contractual agreements which allow third-party suppliers to utilise available capacity at our Baton Rouge transit facility.

CONTRIBUTION TO SUSTAINABILITY

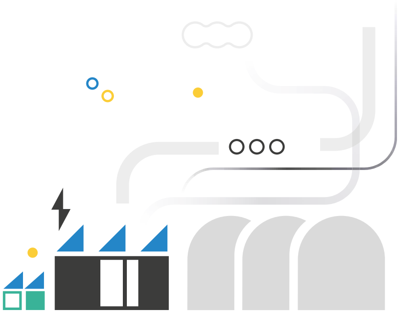
In August 2016, our Morehouse BioEnergy and Amite BioEnergy facilities achieved certification under the Sustainable Biomass Program (SBP) – the leading standard for sustainable production of woody biomass fuels. Drax Biomass is one of only a small handful of US pellet manufacturers to obtain this certification to date. SBP certification, coupled with our continued certification under a variety of forest sustainability schemes, will help differentiate Drax Biomass from other pellet manufacturers as we pursue new supply agreements in new markets.

Risks and mitigations

Weather-related damage to facilities	We carry business interruption insurance to protect against significant losses
Fire/explosion hazard from combustible pellet dust	We employ advanced fire detection and suppression systems at both manufacturing sites and port facility
Disruption in fibre supply from increased competition	We enter into long-term contracts with our suppliers where possible, and we are implementing a portfolio-based approach to our fibre procurement strategy
Regulatory and political change	We actively engage with regulators and legislators at the state and federal levels to influence policy that impacts our markets

Andy Koss
Chief Executive
Drax Power

Contract for Difference (CfD) clearance completes the biomass transformation programme to convert three of our six generating units and provides the foundation for our Generation growth strategy.



MARKET CONTEXT

Drax Power Station is the largest power station in the UK (almost twice the size of the next largest) and continues to meet some 7% of the UK's electricity needs. The key factors influencing our business are the regulatory framework, commodity markets, network generating capacity, and our operational performance.

REGULATORY FRAMEWORK

2016 represents the first full year of operations following the removal of the Climate Change Levy (CCL) exemption for renewable electricity generation on 1 August 2015. The impact of this change was a reduction in 2016 EBITDA in the region of £34 million.

EU approval of the CfD investment contract for our third biomass conversion (signed in April 2014) took longer than expected during 2016. Our original expectation was for approval in early autumn, with the final decision actually coming on 19 December.

New emissions limits came into effect on 1 January 2016 under the Industrial Emissions Directive (IED). Our plant performance has been excellent in this area, and the significant investment in emissions abatement technology has allowed us to run the plant flexibly, as we wished, while staying within our annual allowance. We continue to look at ways to improve our emissions performance.

COMMODITY MARKETS AND GENERATING CAPACITY

Our profitability remains primarily influenced by the bark spread (the difference between the power price and the cost of biomass net of renewable support) and the dark green spread (the difference between the power price and the cost of coal and carbon, including CO_2 allowances under the EU Emissions Trading Scheme and the UK Carbon Price Support (CPS) mechanism).

During 2016, persistently low oil and natural gas prices, combined with warm winter weather, have kept wholesale electricity prices in the UK subdued. However, this year did see the first tangible signs of a capacity squeeze in the UK market, and day-ahead baseload power prices saw several periods of significant volatility, trading for prices in excess of £150 per MWh during November. In 2016, the average price was £48 per MWh sold.

Our flexibility and ability to respond to the demands of the network in these periods has helped to deliver significant value in 2016.

Going forward, CfD approval will help to reduce our exposure to fluctuations in commodity markets. In addition, provision of ancillary services and capacity market income (expected to commence from 1 October 2017) help to provide a more robust and diversified earnings base.

OPERATIONAL REVIEW

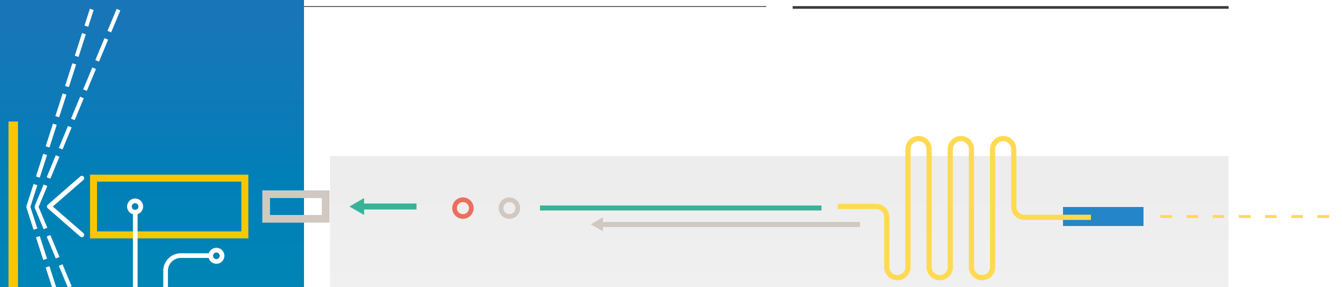
The business has delivered strong operational and commercial performance in the face of significant challenges.

2016 has seen the largest scope of maintenance work the station has ever tackled with 4.6 million man hours worked. The safe execution of so much additional and complex work is a great credit to all those involved, a Total Recordable Injury Rate for the year of 0.13 being testament to this.

In addition to the planned maintenance programme, the entire organisation has responded to a number of unplanned events. The management of these events requires seamless teamwork between the operational, commercial and back office functions to protect value.

The delivery of excellent cross-team working is required in all aspects of our business. This allows us to capture value through flexibility; examples include sourcing and processing non-standard fuels and capturing value in the short-term power markets.

We have also continued to develop a cost and value conscious culture. The business has utilised systems such as Lean, ideas forums and targeted profit improvement initiatives to deliver material value.



KEY PERFORMANCE INDICATORS

12.7TWH

Biomass generation

6.9TWH

Coal generation

£48

Average achieved power price per MWh sold

TECHNOLOGY

SUMMER IN THE STATION

What happens in the summertime at the UK's largest power station?

Electricity demand is lower in the summer, so the assumption would be that activity at Drax Power Station is minimal. The reality, however, is very different. The fall in demand is an opportunity to perform crucial maintenance work – to invest, upgrade and extend the life of our power station and prepare for the winter months.

To carry out major repairs, large sections of the power station need to come offline – this is called an outage. "We run a schedule where each of our six 645 MW units has a major outage every four years," says Andrew Squires, Outage Manager. 2016 was a particularly busy year, with two such outages and four smaller ones for essential repair works.

Carrying out the huge volume of work required to shut down and maintain the units – systems of conveyors, mills, burners, boilers, pipes, cables and turbines – meant that 3,500 people were working at the power station, including a large number of engineering contractors. "It's a number we've never seen previously," Andrew says.

As Europe's largest decarbonisation project, maintaining our biomass units has presented us with new challenges. "We're understanding the engineering implications of using biomass in our boilers, and developing strategies for maintenance," says Andrew.

Original story at: http://www.drax.com/technology/summer-in-the-station-2/

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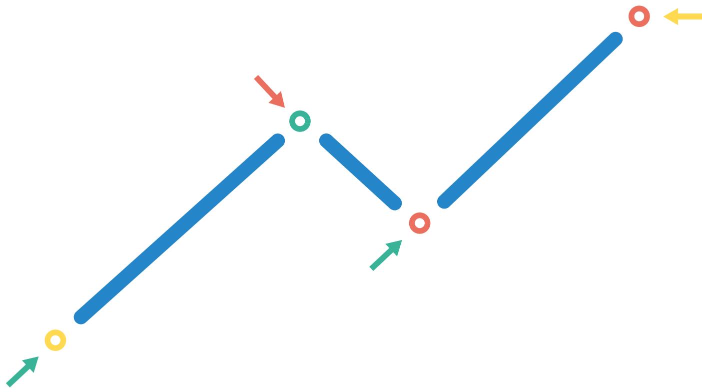

FINANCIAL RESULTS

To end the year ahead of internal targets given the challenging trading, operational and regulatory conditions, in particular the timing of the CfD, represents an excellent performance. The negative impact of the delay in CfD approval and unit availability issues has been offset by:

1) prompt market and system balancing activity which played to our strengths; and demonstrated, yet again, our importance to the Grid to ensure system stability; and
2) the decision by National Grid to award the business a new 12-month black start contract demonstrating the value of Drax in helping to keep the UK electricity system robust.

Gross profit for 2016 was £337 million compared to £390 million in 2015. This reduction includes the impact of lower power prices, lower generation and the removal of the CCL exemption and this was mitigated by prompt market and system balancing activity and the new 12-month ancillary services contract.

DRAX POWER FINANCIAL PERFORMANCE

	2016 £m	2015 £m
Revenue	2,490.9	2,638.2
Cost of power purchases	(904.4)	(843.5)
Grid charges	(69.4)	(84.1)
Fuel costs	(1,180.1)	(1,320.5)
Cost of sales	(2,153.9)	(2,248.1)
Gross profit	337.0	390.1
Operating costs	(163.2)	(175.5)
EBITDA	173.8	214.6

"

2016 HAS SEEN THE LARGEST SCOPE OF MAINTENANCE WORK THE STATION HAS EVER TACKLED; WE HAVE COMPLETED 4.6 MILLION MAN HOURS.

At an operating cost level, we have contributed to a reduction in Group costs, despite the unprecedented level of on-site work described above.

As a result, EBITDA for the year was £173.8 million (2015: £214.6 million).

LOOKING AHEAD

Our objective remains to run a reliable, flexible and profitable generation business. An important part of this is working as a team to execute agile decisions and capture value in a market where grid stability is becoming increasingly important. In addition, following the purchase of four sites with the potential for us to build 299MW Open Cycle Gas Turbines (OCGTs), the business has initiated the process to diversify our generation earnings.

CONTRIBUTION TO SUSTAINABILITY

Sustainability has guided our business purpose for over four decades. We have evolved and innovated to meet the changing needs of society. During the 1980s we invested in desulphurisation equipment to clean up coal, in 2003 we invested in research and development to assess whether biomass was a sustainable fuel of the future. Today we have converted three units to burn biomass which now accounts for 65% of our total output.

Looking ahead, our coal units are expected to end operations by 2025, while investment in OCGTs will act as an enabler for other forms of renewable energy, particularly wind and solar power. Our business purpose directly tackles a number of the UN's sustainable development goals endorsed by 193 governments.

Risks and mitigations

Regulatory risk	We engage with key regulatory stakeholders in government to continue support for biomass within renewables incentives regimes.
Plant risk	We target investment to deliver a safety first operation which is reliable and flexible. The plans are responsive to evolving running patterns and build on experience of operating converted units, including strategic spares and insurance.
Biomass sourcing and operations risk	We have long-term contracting plans and continue to strengthen relationships with suppliers. To complement this we can access spot markets. Flexible contracting, with regular sampling and inspections, secures a reliable and sustainable supply of good quality fuel to support high load factors.
Commodity and FX market price risk	We have a progressive hedging strategy with forward power and Renewable Obligation Certificate (ROC) sales combined with purchases of fuels. This is supplemented by the FX hedging strategy.
Capturing prompt market value and network services	We actively engage with National Grid to offer system services. We maintain flexible, reliable station operations to target near-term trading and balancing market opportunities.

Key Performance Indicators

Area	KPI	Unit of measure	2016	2015
People	Safety	TRIR	**0.13**	0.26
Economic	Biomass generation	TWH	**12.7**	11.5
Low carbon future	Carbon intensity	Tonnes/GWH	**297**	474
Security of supply	Availability	%	**77.1**	85.1

Jonathan Kini
Chief Executive
Drax Retail

We have delivered strong performance across the retail market in an increasingly challenging environment.

DIVISIONAL STRATEGY

2016 was an important year for Haven Power with the appointment of Jonathan Kini as CEO. The strategic focus of Haven is to challenge the market and how customers use power, through our unique ability to provide reliable and renewable energy generated using biomass technology.

As the main part of the Retail arm for Drax Group, Haven supplies electricity to business customers offering 100% renewable electricity, competitive pricing, first-class customer service, and contracts tailored precisely to their needs.

The Haven strategy is to:

– Inspire change so that energy becomes part of a bigger sustainability agenda; it is not just about the kind of energy used, it is also about the way energy is used. The ambition is to make sustainability in energy second nature.
– Work with customers to manage their energy consumption.
– Meet customer demands to deliver renewable energy.

Haven's customer base is both the Industrial and Commercial (I&C) and small and medium-sized enterprises (SME) markets.

Haven provides value for the Drax Group through the provision of an alternative credit efficient route to market for the power, ROCs and Renewable Energy Guarantees of Origin earned when Drax generates renewable power.

Billington Bioenergy (Billington) remains one of the leading UK suppliers of ENplusA1 biomass wood pellets for heating to domestic and business customers. Billington supports the Group's continued position that there is significant potential for biomass within the UK market for heating purposes, aligned with the UK Government's policy objective to decarbonise heat over the next decade.

MARKET

The business sector of the electricity supply market has continued to be very competitive with our established competitors being joined by new entrants.

We are continually improving our service, enhancing relationships with our customers, and providing the products and propositions UK business needs, and so increasing the value that Haven provides to the Group.

The renewable heating market is gaining traction and has benefitted from Government support under the Renewable Heat Incentive (RHI).

The focus of Billington is on the secure and reliable supply of consistent quality heating pellets, delivered with excellent customer service. This is supported by a robust sustainable purchasing strategy, strategic stock holdings, and a well-positioned depot network. Market growth has been driven primarily by the RHI, which the Government has confirmed will continue to be supported through to 2021, encouraging consumers to adopt renewable forms of heating, such as biomass, and move away from fossil fuel heating systems (primarily heating oil and liquefied petroleum gas).

DRAX RETAIL FINANCIAL PERFORMANCE

	2016 £m	2015 £m
Revenue	**1,326.4**	1,290.0
Cost of power purchases	**(688.9)**	(710.2)
Grid charges	**(310.4)**	(285.4)
Other retail costs	**(303.6)**	(275.1)
Cost of sales	**(1,303.0)**	(1,270.7)
Gross profit	**23.5**	19.3
Operating costs	**(27.8)**	(25.6)
EBITDA	**(4.3)**	(6.3)

TECHNOLOGY

SMART METERS

How the energy we use to power and heat our lives is tracked, recorded and fed back to utility companies is changing. It could mean lower bills and a more stable energy network and it's all thanks to smart meters. It's a simple piece of technology that can have a serious impact on how you use energy and how much you pay for it.

We are currently investing in technology to allow us to use the new national smart metering infrastructure. Haven will roll out smart meters to its customers between 2017 and 2020.

Billington has installed smart meters – known as fuel level measurement systems – in care homes and schools and projects that a third of its bulk-blown pellet customers will have them installed by 2020.

Original story at: http://www.drax.com/technology/smart-meters-will-change-use-power

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KEY PERFORMANCE INDICATORS

14.6TWH

Retail power sales volume at customer meter

6%

Year-on year retail power sales volume growth

21%

Year-on-year Gross Margin growth

Risks and mitigations

Regulatory and political risk	Where possible we seek to work closely with and influence regulatory and other bodies
Credit risk	We have well-developed credit checking and monitoring procedures
Commodity market price risk	We have well-developed hedging policies which are kept under review for market developments
Operating risk	We have business continuity plans in place which are regularly reviewed and tested

OPERATIONAL REVIEW

An excellent standard of customer service is central to our retail business proposition.

This good service reputation has supported retention levels. Haven was named Supplier of the Year at the UK's Energy Awards 2016, as a result of our focus on energy efficiency, customer service and customer partnerships.

We actively manage credit risk by assessing the financial strength of customers and applying rigorous credit management processes. A strong focus continues to be placed on billing and cash collection which has resulted in the retail business being a net contributor of cash to the Group.

FINANCIAL REVIEW

Movements in key financial metrics are underpinned by continued growth in the retail business and changes in average prices. For the period in question Haven delivered net sales volume growth of 6% to 14.6TWH (2015: 13.8TWH) and gross margin growth of 21% to £23.5 million (2015: £19.3 million).

The volume growth continues to be from the larger I&C market. Many of our larger customers are signed up to flexible contracts where the customer decides when to fix the price of their power, or to leave it to day or month ahead prices. The lower wholesale power prices have therefore impacted on the average sales price for 2016.

Third Party Costs (TPCs) include grid charges, the cost of meeting our obligations under the Renewable Obligation (RO) and small-scale Feed-in-Tariff schemes. Grid charges include distribution, transmission and system balancing costs. TPCs have continued to increase and now account for 46% of revenue.

The markets have continued to remain very competitive. A focus on sourcing, products and services during 2016 contributed to the gross margin growth.

Billington also delivered strong sales volume growth. Margins were in line with expectations of the business for this stage of its development.

These factors resulted in a reduction of the Retail EBITDA loss to £4.3 million (2015: 6.3 million).

SUSTAINABLE BIOMASS IS AT THE HEART OF OUR SMART SOLUTIONS

DRAX'S SUSTAINABILITY GOVERNANCE

Drax Group only ever uses biomass that is sustainably produced and legally sourced. We have set ourselves clear requirements in our sustainability policy. In addition we adhere to the UK Government's criteria for sustainable biomass. Our dedicated sustainability team reports to the Group Head of Sustainability and they ensure our biomass meets all these requirements.

By achieving this, Renewable Obligation Certificates (ROCs) can be claimed for the electricity we generate from compressed wood pellets instead of coal.

OUR SUSTAINABILITY POLICY

The biomass we use to generate electricity is at the heart of our business. Because this must be sustainable, we always strive to make sure that all of the pellets we use comply with our policy:

- Significantly reduce GHG emissions compared to coal-fired generation.
- Contribute to local prosperity in the area of supply chain management and biomass production.
- Not endanger food supply or communities where the use of biomass is essential for subsistence (for example heat, medicines and building materials).
- Contribute to the social wellbeing of employees and the local population in the biomass producing areas.
- Not adversely affect protected or vulnerable biodiversity and, where possible, give preference to biomass production that strengthens biodiversity.
- No net release of carbon from the vegetation and soil of either forests or agricultural land.
- Deploy good practices to protect and/or improve soil, water (both ground and surface) and air quality.

WHAT ARE THE UK GOVERNMENT'S SUSTAINABILITY LEGISLATION CRITERIA?

Drax claims ROCs for electricity generated by biomass. To do so we must show that all the biomass we consume meets both the sustainability and Greenhouse Gas (GHG) emissions savings criteria set out by the UK Government. In summary form, these require that management of the forest from which the biomass was harvested must ensure:

- harm to ecosystems is minimised;
- productivity of the forest area is maintained;
- bio-diversity is maintained and protected;
- the health and vitality of the ecosystem is maintained;
- customary and legal rights, including health and safety standards, are observed.

WHAT ARE WE DOING TO MAKE SURE OUR BIOMASS IS SUSTAINABLE?

Drax is working to ensure the delivery of sustainability is improved along the entire length of our supply chain. We work to improve forestry practices in the places from which we source the raw materials for our wood pellets and to reduce the impact of our sourcing right up to the moment they are fed into our generating units. This responsibility covers three key areas: environmental, social and economic. This requires us to develop good working relationships with all the partner organisations with whom we work so that we can identify and develop solutions to any issues that arise in the process, and that we can help our partners improve the way they work.

HOW DO WE ENSURE THE SUSTAINABILITY OF BIOMASS FROM THIRD-PARTY SUPPLIERS?

Our contract with any proposed biomass supplier stipulates that they must make a sustainability declaration that provides key information about: the areas from which their raw materials come; forest management practices in those areas; and the GHG characteristics of their pellet manufacturing plant and their biomass supply chain.

We then require the proposed supplier to undergo an audit carried out by an independent third party on the ground. This involves checking information provided in their declaration and regional analysis against both our own Sustainability Policy and the regulatory criteria set out by the UK Government.

This rigorous process demands that the independent auditor investigates the forest management practices in the areas from which the supplier sources their raw material.

For a new supply it is only when this process has been completed, and we can be sure that the wood pellets the proposed supplier provides will satisfy all our policy and regulatory standards, that they can be approved as a supplier to Drax.

Then, every year, all approved suppliers are required to submit up-to-date information and data for review in order to demonstrate the continued sustainability of their operations. Independent auditing then continues as part of a regular cycle of supervision (usually once every three years but more often if required).

Sustainability can also be demonstrated through forest management certification. This shows that responsible forestry is being practised in the forests where the raw materials are sourced. To achieve forest management certification the forest and management practices must be audited and endorsed by independent third parties.

WHAT DOES THE SUPPLIER AUDIT INVOLVE?

Drax's sustainability audit requires the supplier pass no fewer than 107 detailed checks along the whole length of their supply chain and pellet manufacturing process. Negative findings are categorised into three priorities: high, medium and low. High-priority findings can result in termination of our agreement. Medium-priority findings result in the supplier being given a set timescale within which to rectify them.

OUR PRINCIPLES

01 We never work in countries that lack proper regulation.

02 We never cause deforestation or forest decline.

03 We never source from areas that are officially protected or where our activities harm endangered species.

04 We only take wood from working forests that grow back and stay as forests.

05 We require all our suppliers to pass tough screening and sustainability audits, conducted by independent auditors.

Low-priority issues highlight areas where our independent auditors believe suppliers have room to improve their practices, though all requirements are being met.

Twelve new pellet mills and eight existing suppliers were audited through this independent process in 2016. The auditors noted 1 high-priority issue, 23 medium-priority issues and 40 improvement opportunities. On discovery of the high-priority issue, we did not contract with the supplier. Of the 23 medium-priority issues, 14 are complete, four are in progress and five are yet to be actioned.

WHY SUSTAINABLE FOREST MANAGEMENT MATTERS

Sustainable forest management (SFM) requires environmentally appropriate, socially beneficial, and economically viable management of forests for present and future generations.

Drax sources biomass only from productive working forests. Sustainable management of working forests provides a wide range of benefits.

Economic benefits: Increased productivity and quality due to better management practices, improving planting material (seedlings), weed control and fertilisation, ground preparation and drainage, appropriate thinning to provide more high-value wood. This can increase revenue for the forest owner and encourage investment in the forest resource and ensure that the long-term future of the forest is secured (as opposed to conversion to other more lucrative land uses e.g. cotton or urban development).

Sustainable logging cycles – planning harvesting and replanting operations according to the age and growth rate of the forest – can ensure that a regular supply of wood is available now and in the future. Harvesting programmes can be managed for long-term benefit and sustainable supply.

Environmental benefits: By practising SFM, habitat diversity is preserved and sensitive sites protected.

Well-managed forests also help to protect and conserve water sources and soil quality, reduce the risk of damage from fire, pest or disease and increase the rate of carbon sequestration and storage. In the US South, the growing stock (volume of timber/total amount of carbon) of the forest has more than doubled in the last 60 years as a result of improved forest management practices, whilst the total area of forest has remained largely the same.

Social: SFM also provides greater social benefits often offering a greater degree of public access with the provision of nature trails, mountain bike routes, picnic areas and wildlife observation areas. Actively managing a forest provides benefits to the local economy and related industries including increased local employment. It also contributes to the visual quality of the landscape.

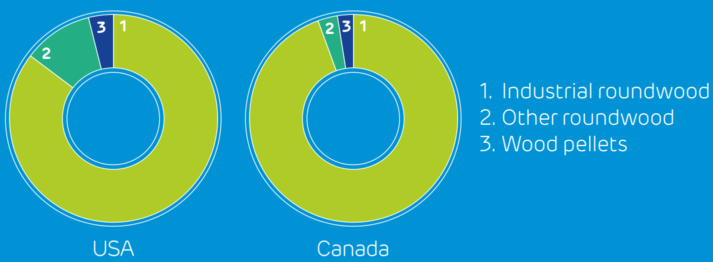
4.6M TONNES

of Drax feedstock came from controlled wood sources in 2016

ROUNDWOOD AND BIOMASS PRODUCTION IN NORTH AMERICA

In 2015 almost 400 million cubic metres of roundwood (all harvested wood for industrial and fuel usage) was harvested in the US for use in the forest products industry for construction, furniture, paper, composite board production and woodfuel. Of this wood fibre less than 4% was used to make wood pellets and only 2.4% was used for export pellets. In Canada 156 million cubic metres was harvested and only 2.6% was used for wood pellet production. This clearly shows that the wood pellet sector is a very small part of the overall market for wood products.

North American production of roundwood and pellets 2015 (%)



CHAIN OF CUSTODY AND FOREST CERTIFICATION

Forest management (FM) certification is one of a range of methods to confirm, through independent third party audit, that a specific area of forest is being managed in accordance with a particular standard or agreed set of principles and criteria. Once achieved, FM certification allows the forest owner to readily demonstrate their sustainability credentials and management standards. In 2016 Drax's suppliers sourced more than 1.5 million tonnes of wood fibre from FM certified forests.

FM certification may be difficult to achieve for some type of forest owners. That is why a secondary level of assessment called Controlled Wood is available for wood procurement organisations. This ensures that wood fibre is NOT:

- illegally harvested;
- harvested in violation of traditional and human rights;
- harvested in forests in which High Conservation Values (HCVs) would be threatened by management activities (HCVs are areas particularly worthy of protection);
- harvested in forests being converted to plantations or non-forest use;
- from forests in which genetically modified trees are planted.

In 2016 4.6 million tonnes of Drax feedstock came from controlled sources.

Once certified, Chain of Custody (CoC) can be used as a mechanism for tracking wood fibre from the forest to the final product and destination. Each supplier in the chain must have a documented system to be able to identify and trace the wood fibre at each stage. Drax requires that all of its suppliers achieve CoC certification.

"

THE AMOUNT OF CARBON SEQUESTERED FROM A FOREST IS DIRECTLY RELATED TO THE GROWTH RATE OF THE TREES. SO THE HIGHER THE RATE OF GROWTH THE MORE NEW CARBON IS SEQUESTERED.

ACTIVE FOREST MANAGEMENT AND CARBON STORAGE

The amount of carbon sequestered from a forest is directly related to the growth rate of the trees. So the higher the rate of growth the more new carbon is sequestered and the greater the rate of absorption from the atmosphere.

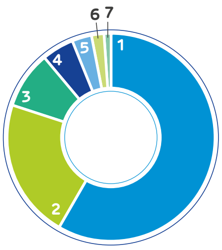
Mature trees have a high carbon stock (the amount of stored carbon) but a low rate of absorption. Younger trees are much more effective at removal of CO_2 from the atmosphere.

If old stands of trees are not harvested their rate of carbon absorption will plateau, limiting their ability to impact on atmospheric carbon.

Harvesting mature trees from working forests when their growth rate has slowed and replacing them with young vigorous trees has a much better impact on atmospheric carbon, especially if much of the high-value wood harvested is stored in long-term wood products (construction, furniture etc.).

Biomass is a by-product of this process. Produced either in the removal of thinnings, or as the low-grade roundwood left over after sawlogs have been harvested, or as residues from harvesting or at the sawmill. Drax does not take any wood from primary forest or highly bio-diverse forest areas.

Drax biomass country of origin 2016



1. USA – 59%
2. Canada – 22%
3. Latvia – 9%
4. Estonia – 5%
5. Portugal – 3%
6. UK – 2%
7. Other EU – 1%

BIOMASS PELLET FEEDSTOCKS

Our biomass pellets are sourced from North America and Europe. Drax is required to report all feedstock categories to the Office of Gas and Electricity Markets (Ofgem) in accordance with their guidelines and criteria. This information can be found at: www.ofgem.gov.uk

COUNTRIES OF ORIGIN AND FEEDSTOCKS OF OUR BIOMASS PELLETS

The following table shows the types of feedstocks we used in 2016 by weight (tonnes) and country of origin.

	Sawmill residues tonnes	Branches, tops and bark tonnes	Diseased wood and storm salvage tonnes	Thinnings tonnes	Low grade roundwood tonnes	Agricultural residues tonnes	Total tonnes
USA	861,083	752,659	9,583	1,413,566	852,544	2,496	3,891,931
Canada	1,125,010	186,611	–	7,393	102,355	–	1,421,369
Latvia	345,365	37,648	809	37,723	161,994	–	583,540
Estonia	215,740	–	–	46,351	94,073	–	356,164
Portugal	32,975	43,438	3,529	33,603	52,385	–	165,930
UK	–	–	–	–	–	133,606	133,606
Other EU	37,637	161	6	827	10	–	38,640
Total	**2,617,811**	**1,020,517**	**13,927**	**1,539,463**	**1,263,361**	**136,101**	**6,591,180**

DEFINITIONS:

Sawmill residues: wood residue in the form of chip, bark, sawdust, etc. that is produced at a sawmill.

Branches, tops and bark: material produced from harvesting that cannot be used for other markets.

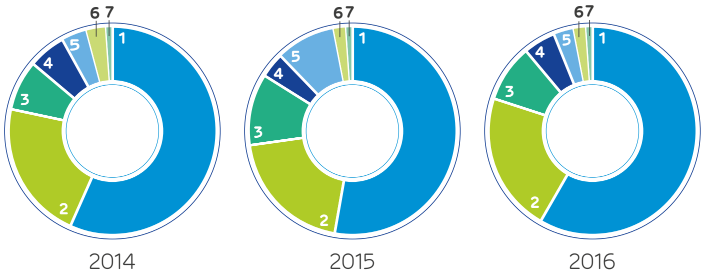
Diseased wood and storm salvage: timber that is diseased or has been damaged during a storm.

Thinnings: roundwood from a forest or plantation thinning, where the main objective is to reduce the density of trees in a stand and improve the quality and growth of the remaining trees.

Low-grade roundwood: stemwood of any size or length that is not suitable for, or cannot access, higher value markets.

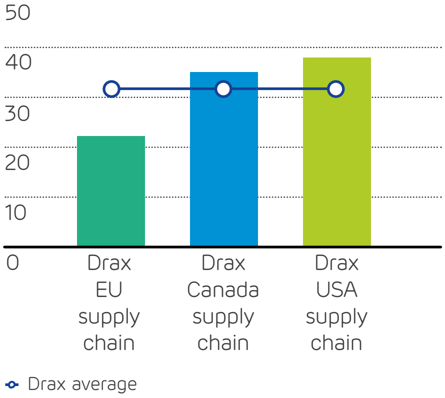
Agricultural residues: residues from agricultural production (e.g. straw, peanut husks), or purpose-grown energy crops (miscanthus).

Drax feedstock mix for years 2014–16 (%)



2014	2015	2016
1. USA – 58%	1. USA – 53%	1. USA – 59%
2. Canada – 22%	2. Canada – 20%	2. Canada – 22%
3. Latvia – 8%	3. Latvia – 11%	3. Latvia – 9%
4. Estonia – 6%	4. Estonia – 4%	4. Estonia – 5%
5. Portugal – 4%	5. Portugal – 9%	5. Portugal – 3%
6. UK – 3%	6. UK – 2%	6. UK – 2%
7. Other EU – 1%	7. Other EU – 1%	7. Other EU – 1%

Drax biomass supply chain GHG emissions (CO_2 EQ/MJ)



33.9 CO_2 EQ/MJ

2016 average biomass Supply chain GHG emissions

SUPPLY CHAIN GHG EMISSIONS

The Renewables Obligation sets out the basis on which Drax is required to determine and report on the life cycle GHG emissions associated with its supply chain. Every supplier is required to give detailed information on what type/s of fibre is/are used to make wood pellets along with full details of their sources, the distances and vehicle types involved in their production, the production process itself, data about fuel and energy usage, plus any sea-freight data (including what type of vessel was used, over which route, over what distance). This data is entered into the BEIS (formerly DECC) solid biomass and biogas carbon calculator and used to determine the precise level of supply chain GHG emissions associated with an individual biomass supply. Information about these levels is reported to Ofgem.

The UK Government has set a limit on the maximum supply chain GHG emissions permitted in order for biomass to be eligible for support under the RO. The current limit for CO_2 emissions from life cycle analysis of biomass supplies is 79.2 g CO_2(e)/MJ – reducing to 50 g CO_2/MJ by 2025.

In 2016 the average supply chain GHG emissions from all of Drax's biomass supplies amounted to 33.9 g CO_2 (e)/MJ. The UK Government has provided a benchmark figure for GHG emission from coal which is 250.8 g CO_2 (e)/MJ, therefore in 2016 Drax saved around 86% of CO_2 (e) emissions compared to the coal benchmark.

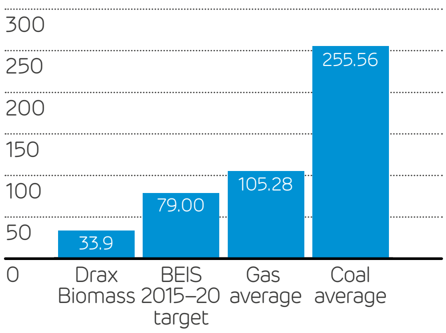
GHG emissions are affected by a wide range of factors including cultivation, harvesting and transportation. For Drax the majority of our pellets are shipped to the UK from North America.

The impact of shipping emissions is determined by both distance and vessel size. For longer distances (e.g. from North America) it is essential to use large-scale vessels capable of transporting more than 40,000 tonnes of wood pellets each time (sometimes up to 60,000 tonnes); this significantly reduces the emissions per tonne of wood pellets. Within Europe shipping distances are much shorter and therefore smaller vessels can be utilised, which also allows vessels to access small ports that can reduce inland transportation.

Drax uses specially designed rail wagons to transport the biomass pellets direct from port to power station. This is dramatically more carbon efficient than road transport.

THE AMOUNT OF CARBON SEQUESTERED FROM A FOREST IS DIRECTLY RELATED TO THE GROWTH RATE OF THE TREES. SO THE HIGHER THE RATE OF GROWTH THE MORE NEW CARBON IS SEQUESTERED.

Life cycle emissions 2016 (CO_2 EQ/MJ)



Calculated using Ofgem's Solid and Gaseous Biomass Carbon Calculator.

Source: DUKES/2015 (Digest of UK Energy Statistics)

SUSTAINABLE BIOMASS PROGRAM

The Sustainable Biomass Program (SBP) is an independent certification scheme designed to assure that woody biomass has been legally and sustainably sourced.

In 2016 Drax achieved CoC certification for the procurement of wood pellets for the generation of electricity and heat under the SBP certification scheme. This enables us to more effectively demonstrate the sustainability of our wood pellet supplies. Drax will continue to support SBP and continue to encourage wood pellet suppliers to achieve certified status.

Ofgem assessed SBP in 2015 and found that it met all of the sustainability criteria laid out by the UK Government. More information can be found at www.sustainablebiomasspartnership.org

COAL SOURCING

As we have upgraded half the power station to produce electricity from wood pellets, clearly our need for coal has reduced. However, it is important that we continue to secure reliable coal supply from known sources and from jurisdictions and counterparties that are vetted against our various compliance policies. We avoid buying "generic" coals, where the origin can be uncertain, either bilaterally or over trading platforms.

Coal sourcing is overseen by our Compliance, Sustainability and Risk teams and we carry out appropriate due diligence around our coal sourcing. Where our checks raise any "red-flags" we undertake further targeted due diligence and will ultimately engage with Drax's Ethics and Business Conduct Committee if that is deemed necessary.

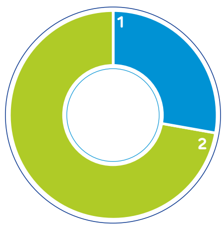
We buy coal from a range of sources with the objectives of managing our commercial exposures, environmental obligations and diversity of supply. In 2016, 28% of the coal we used came from UK deep and surface mines with the remainder coming from major supply basins around the world, including the US and Colombia.

When buying from overseas we have continued to require, through our contracts, that suppliers meet standards in respect of compliance with legislation, human rights, labour relations and health and safety arrangements. To this end Drax is an active member of an initiative called Bettercoal. This is a not-for-profit organisation founded by a number of major European coal generators that sets out to encourage mining companies to demonstrate that they operate in a socially responsible way.

COAL SOURCING BY COUNTRY

Country	Tonnes
Colombia	1,865,682
US	75,726
UK	770,680
Total	**2,712,087**

Coal sourcing by indigenous and imports for the year 2016



1. UK – 28%
2. Imports – 72%

SMART SOLUTIONS FOR THE ENVIRONMENT

Sustainability and protecting the environment are crucial to Drax and the local communities in which we operate. Environmental compliance at Drax Power Station and the ash disposal site associated with it is managed under an environment management system. This system is now externally validated and certified to the new international standard ISO 14001 2015. It is audited twice every year.

Over the last 12 months, Drax Power Station has continued its drive to manage its impact on the environment, whether that be carbon, NOx, sulphur dioxide, particulate emissions into the atmosphere, use of water or waste to landfill.

There have been no major breaches to our environment consents in 2016.

Emissions to air

Drax's carbon reporting in accordance with the Companies Act 2006 and the European Union Emissions Trading System (EU ETS) is shown in Table 1.

Scope 1 accounts for emissions produced by the combustion of coal, heavy fuel and propane – to generate electricity, along with the operation of certain plant at the power station, i.e. the flue gas desulphurisation system.

Scope 2 accounts for emissions mainly attributed to electricity purchased to run operations across our various sites. These emissions are measured using the Greenhouse Gas Protocol, a Corporate Accounting and Reporting Standard (revised edition) and the Government's published GHG conversion factors.

We are also required to disclose emissions from biologically sequestered carbon, which includes emissions released through the combustion of biomass to generate electricity. These emissions are shown in Table 2. The figures do not take into account the CO_2 that has been absorbed from the atmosphere during the growth of feedstocks which are used to manufacture the biomass pellets used at Drax to generate electricity.

The biogenic CO_2 emissions resulting from power generation are counted as zero in official reporting to both UK authorities and under the EU ETS as the use of sustainable biomass is considered to be carbon neutral at the point of combustion. This methodology originates from the United Nations Framework Convention on Climate Change (UNFCCC).

The majority of our emissions result from the process of using solid fuel. This can make it difficult to identify other smaller trends that are still significant. To offset this dominance and to ensure we retain a balance between highlighting significant developments and providing meaningful data, we have adopted a materiality threshold of 100,000 tonnes of CO_2.

Table 3 sets out Drax total electricity generation and the emissions per GWH of electricity generated by fossil fuel combustion.

Reducing CO_2 emissions

A principal indicator of Group performance is CO_2 emissions, calculated under the EU ETS as a ratio of electricity generated before deductions used on site.

Independently verified CO_2 emissions at Drax Power Station have fallen from 13.3 million tonnes in 2015 to 6 million tonnes in 2016. That's a decrease of more than 53%.

This fall is largely due to the conversion of three of our six generating units to be fully powered by sustainable biomass rather than coal.

TABLE 1
FOSSIL FUEL, OPERATIONS AND PURCHASED ELECTRICITY EMISSIONS

Activity	Unit of measure	2016 kt	2015 kt	2014 kt	2013 kt	2012 kt
Scope 1						
Fossil fuel combustion	KT	**6,021**	13,101	16,476	20,162	22,513
Operations	KT	**<100**	<100	119	157	180
Total Scope 1	KT	**6,021**	13,101	16,595	20,319	22,693
Scope 2						
Purchased electricity	KT	**151**	216	249	293	341
Total Scope 1 and 2	KT	**6,172**	13,317	16,844	20,612	23,034

TABLE 2
BIOLOGICALLY SEQUESTERED CARBON (BIOMASS COMBUSTION) EMISSIONS

Activity	Unit of measure	2016 kt	2015 kt	2014 kt	2013 kt	2012 kt
Biologically-sequestered carbon (biomass combustion)	KT	**11,455**	10,238	7,150	2,799	1,214

TABLE 3
TOTAL EMISSIONS PER GWH OF ELECTRICITY GENERATED BY FOSSIL FUEL COMBUSTION

Activity	Unit of measure	2016 kt	2015 kt	2014 kt	2013 kt	2012 kt
Gross generation	TWH	**20.8**	28.1	28.5	28.0	29.0
Emissions per GWH of electricity generated	T/GWH	**297.0**	474	591	736	794

Another contributing factor is the changing run rates on our coal-fired units. As these move away from providing constant baseload electricity to providing more flexible support services, they will be running less frequently and for shorter periods, and hence emitting less CO_2.

Alongside carbon dioxide, we also manage all our emissions to the atmosphere and have invested heavily in flue abatement systems to make sure that we comply with all environmental limits. All our emissions in 2016 were within the limits set by the Environment Agency.

TOTAL EMISSIONS (KT)

	2016	2015	2014	2013	2012
Sulphur dioxide	**8.3**	18.5	23.8	31.7	35.1
Nitrogen oxides	**14.7**	31.4	35.5	39.2	39.2
Dust	**1**	0.9	0.9	0.8	0.8

Reducing NOx emissions

The introduction of the Industrial Emissions Directive from January 2016 requires significant reductions in NOx. Drax Power Station has achieved a reduction from 31 kilotonnes in 2015 to around 15 kilotonnes this year.

This has been achieved by a number of factors:

- using biomass rather than coal for generation;
- the installation of new low-NOx burners;
- using low-NOx coal;
- fitting five out of six generating units with selective non-catalytic reduction (SNCR) equipment.

SNCR works by releasing urea into the combustion chamber where it combines with oxides of nitrogen to produce atmospheric nitrogen and water.

PARTICULATES

Particulates released into the environment by Drax Power Station have increased slightly from 0.9 kilotonnes to 1.0 kilotonnes in 2016, but remain well within the permitted limits.

This increase is mainly due to the use of slightly different fuel in the coal-fired generating units. Use of "advantaged fuels", such as pond fines (the filtered residue of coal washings) and ash from biomass that has previously been used in our biomass-fuelled generating units.

USE OF WATER

Drax Power Station uses water from the River Ouse, and smaller amounts from the Sherwood Sandstone Aquifer and town's mains.

The water we abstract is principally used for cooling with some also used within the steam system and ancillary processes, including SNCR. Around half of the water abstracted for cooling is returned to the River Ouse. Procedures are in place on site to manage and monitor drainage and water systems and ensure that all discharge consent limits are met.

Borehole water use has slightly increased since 2015, from 1.7 million tonnes to 2.2 million tonnes. This is mainly due to the use of the SNCR system to reduce NOx emissions, which requires increased supplies of water. This is a temporary increase which will be addressed with the commissioning of the new on-site SNCR water treatment plant.

WATER ABSTRACTION (MT)

	2016	2015	2014	2013	2012
River Ouse water	**52.9**	60.6	62.5	56.9	56.7
Mains water	**0.2**	0.2	0.4	0.3	0.2
Borehole water	**2.2**	1.7	1.7	1.9	1.9
Water utilised on site and discharged to the River Ouse	**28.4**	35.2	34.1	31.5	30.8

WASTE TO LANDFILL

There has been a small increase in waste sent to landfill from Drax Power Station in 2016. The overall percentage of waste not sent to landfill in the past year was 94%. If we remove exceptional projects, the figure remained at 98%, the same as in the previous year.

The largest exceptional project was the removal of the plastic packing material that is used to provide extra surface area for water to evaporate on at the base of the cooling towers at Drax Power Station.

Because we use water abstracted from the River Ouse in our cooling towers, over time this packing material becomes silted up with river mud. This means that it needs periodically to be removed, with the old material sent to landfill and replaced with new packing. 2016 saw just such a replacement, which will not be repeated on that cooling tower for approximately another 15 years. The programme itself is ongoing and other cooling towers will undergo the same treatment over the next 2–3 years.

Drax is one of the first applicants to receive certification under ISO 14001 2015, the revised international standard for environmental management systems. This demonstrates our commitment to and maintenance of the highest levels of environmental management.

PEOPLE AND CULTURE

At the year-end, Drax Group employed a total of 1,488 people. The charts below break down the number of employees across all Group businesses. Almost all our employees are on permanent contracts.

The charts show the split across the whole Group, together with the senior management team (Board, Executive Committee and direct reports). The Board's diversity policy is explained in the Nominations Committee report.

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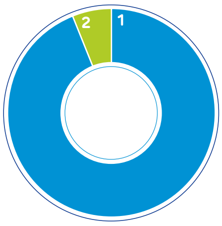
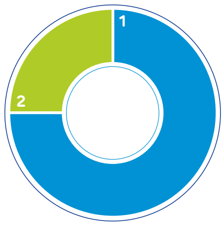
Employment contracts



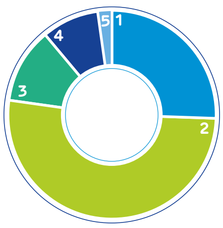
1. Full time – 94%
2. Part time – 6%

Employment gender



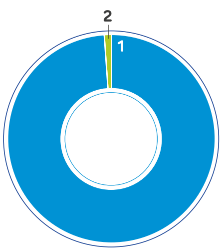
1. Male – 75%
2. Female – 25%

Business unit distribution



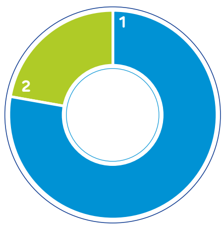
1. Haven Power – 26%
2. Drax Power – 52%
3. Drax Biomass – 12%
4. Corporate – 9%
5. Billington Bioenergy – 2%

Employment status



1. Permanent – 99%
2. Temporary – 1%

Senior management Group gender diversity



1. Male – 78%
2. Female – 22%

EMPLOYEE ENGAGEMENT

We carried out an engagement survey of all our UK and US employees in October 2016. Developed and delivered with Towers Watson, the survey attracted a participation rate of 76% overall. Across all categories of question, the results demonstrated a positive variance compared with the norm for Towers Watson's Global Energy and Utilities surveys.

EMPLOYEE REPRESENTATION

Overall, 37% of the workforce across the Group is covered by collective bargaining. We have representative employee consultation and information arrangements in place for those employees who have individual employment contracts.

We make use of a range of channels to communicate with colleagues and inform them of any important developments in Group operations. We also provide frequent opportunities for employees to feed back.

EMPLOYEE POLICIES AND RELATIONS

All our employees benefit from a range of policies to support them in the workplace. These include policies designed to enable, if appropriate, a range of different work/lifestyle preferences, processes whereby employees can raise grievances or concerns about safety, along with supporting a diverse and inclusive workplace. Drax maintains high standards in employment practices and strives to give employees long-term employment security.

LEARNING AND DEVELOPMENT

2016 saw a number of key developments in this field.

- We successfully launched the Drax Group intranet, making it easier to communicate with one another across the Group, and giving us an online platform through which to share learning.
- We are developing an ongoing learning programme to help individuals and managers through a suite of online and offline resources.

PEOPLE STRATEGY

– We have recently completed our first leadership training programme across our retail businesses.
– We carry out annual performance and development reviews for every employee.
– Every employee benefits from support with his or her personal and career development, helping them develop the technical skills, leadership and management skills and the personal behaviours that will help us drive our Business Plan forward.
– We have strengthened our in-house team in order to support these initiatives and to deliver our HR 2020 strategic plan.

REWARD AND RECOGNITION

Our remuneration and reward packages are regularly checked against benchmarks in our own sector of industry and across the entire market – on either a national or a local level depending on the individual role concerned.

We encourage our UK employees to take ownership of the business in which they work through a range of share plans.

The foundations we are building with our new HR strategy will enable us to take a more holistic view of reward and recognition so that we can create even more personal packages tailored to an individual's needs.

OUR JOURNEY TO 2020

At Drax, we understand that our people are the key to our success now and in the future. To make that success more sustainable, throughout 2016 we have undertaken a root and branch review of our approach to HR across the Group.

Through an extensive consultation process, we have now developed a world-class people strategy that will impact employees at all levels across the Group and take us forward to 2020.

This strategy focuses on three key areas, which will help Drax create a high-performance, sustainable organisation that is optimally placed to deliver our strategic and operational objectives. These three areas are:

– Valuing our people
– Driving business performance
– Focusing on talent

In particular, our new people strategy is designed to enable us to:

– attract and recruit the right people to drive the business forward;
– objectively differentiate between our people;
– leverage expertise across the Group;
– improve cross functional and cross business working;
– adapt and respond to constant change;
– develop and retain a deep pipeline of leadership and specialist talent;
– instil confidence and pride in our employees;
– drive performance.

The solution is not about "one size fits all" as the culture, employee populations and life cycle of each of the Group's businesses differ widely. Rather it's about developing base-level consistency in core areas to allow the Group as a whole to take advantage of an integrated approach to HR.

Working across the four businesses that make up the Group, we have agreed a set of shared HR values.

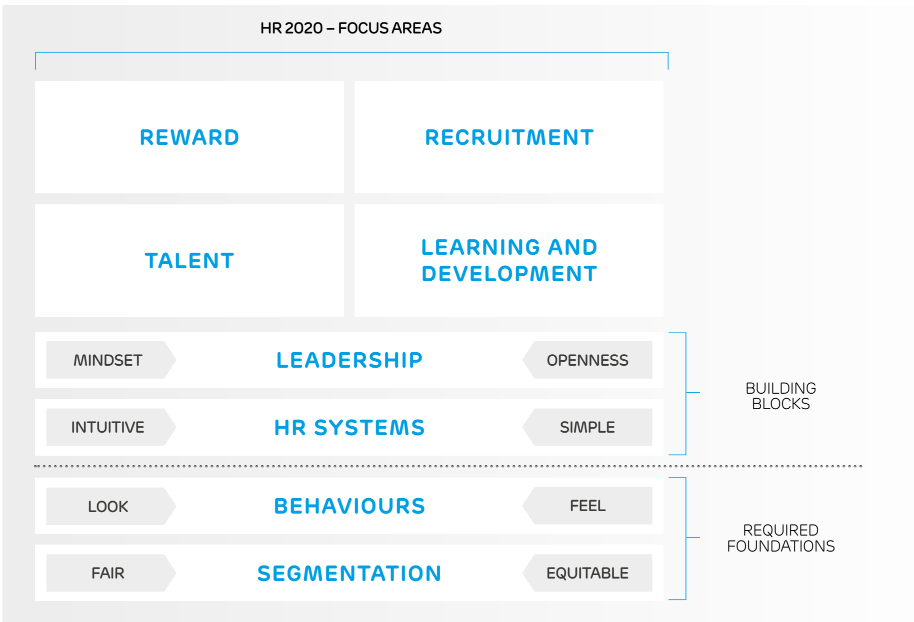
We have also started on delivering a People Plan that will take us through to 2020. As the diagram below shows, this is based around our four main focus areas, supported by the required foundations and building blocks.

This strategy will enable us to develop a culture which values what people do, as well as valuing the way in which they do it.

This new culture will be reflected at every level throughout the organisation, from the systems we use to review performance to the development of learning materials, and will be reflected in the way we reward and remunerate our employees.

By working together across the Group we can better support our employees in all aspects of their working lives, investing in the areas that matter from career and personal development to leadership skills and process efficiency.

We are very much at the beginning of this journey, but we are committed to reaching the end. By fulfilling this commitment, we will give ourselves the best possible opportunity of finding, developing and rewarding the right people to help the Group grow and thrive.



STAKEHOLDER ENGAGEMENT

Drax has a wide and diverse group of stakeholders. These include our shareholders, the people who work for us, our customers, the companies who supply us, the communities in which we work, Government, non-Governmental organisations, regulators, opinion-formers and the media.

We believe it is absolutely vital to communicate effectively with all our stakeholders. It is our aim to be transparent and open in everything we do.

HOW WE COMMUNICATE

We strive to use the most appropriate communications channels to engage all our stakeholders and ensure that everyone can access all the information they need about our policies, practices and strategic direction.

As the world moves increasingly online, in 2016 we have managed a substantial increase in the frequency and volume of our digital communications, because this is the most efficient way to stay in touch, open up a dialogue and to maintain communication with many of our stakeholders.

At the heart of our new digital strategy is the new website for the whole Group, which launched on 6 October 2016. Together with a much greater focus on social media and on creating content about Drax's businesses and the world of energy in general, this has led to dramatically higher levels of engagement by stakeholder audiences.

DRAX'S DIGITAL UNIVERSE

How digital platforms are enabling Drax to engage more stakeholders from more audiences, more efficiently.

30,000

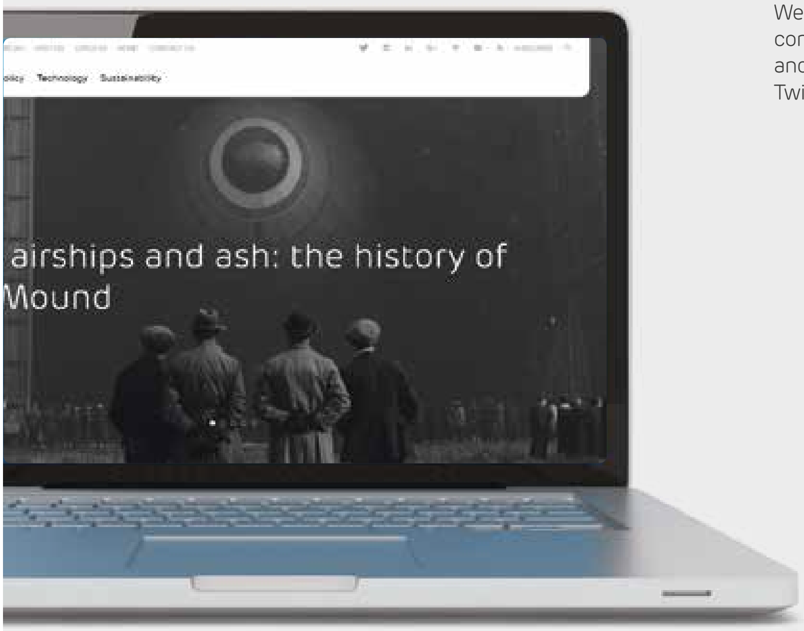
Visitors
Over 30,000 people visited the new Drax website between its 6 October launch and the end of the year.

+108%

The time visitors spent looking at the Investors section of the new website is up 108%[1].

[1] Based on a comparison of the time periods 6 October to 14 December 2015 to 6 October to 14 December 2016 (the new website launched on 6 October)

drax.com



1.2M

Tweets
In the three months to mid-November 2016, our tweets appeared in 1.2 million Twitter user feeds.

Our content was clicked on 3,500 times during this period.

We took part in 174 conversations, received 1,000 likes and were retweeted 825 times.

1,000

Conversations
We've had over 1,000 conversations with individuals and other organisations on Twitter this year.

12,000

Reads
Our Twitter activity drove more than 12,000 reads of Drax content on our websites and LinkedIn.

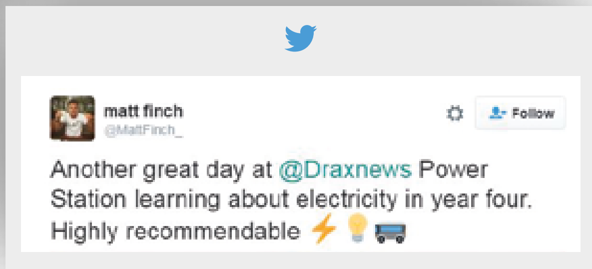
+412%

4,343[2] Twitter users follow @ DraxNews – up from 849 since 1 January – an increase of 412%.

[2] as of 14 December 2016

PROMINENT NEW FOLLOWERS

Leading new Twitter followers over recent months include: Iain Wright MP, Chair of the House of Commons Business, Energy and Industrial Strategy Committee, Public Health and Innovation Minister Nicola Blackwood MP, The Joseph Rowntree Foundation and many journalists.



LinkedIn

100,000

Views
Drax content regularly appears in more than 100,000 LinkedIn users' feeds each month.

Between 1,000–2,000 of those people either click, like, comment or share it.

+28%

Drax has 5,567[3] followers on LinkedIn – up 28% since 1 January when we had 4,347 followers.

[3] as of 14 December 2016

electricinsights.co.uk

4,200

Visitors
4,200 people have visited Electric Insights, a Drax collaboration with researchers at Imperial College London, helping to educate stakeholders about the different technologies generating electricity in Great Britain, their respective roles and their impact.

draximpact.co.uk

1,000

Readers
1,000 people have visited our Drax Impact website since its September launch – this uses data visualisations and case studies to explore our supply chain and its £1.24 billion impact to the UK economy.

BUSINESS CONDUCT

We subscribe to and maintain the highest of ethical standards. We always strive to carry out our business honestly, with integrity and according to the spirit as well as the letter of all applicable laws and regulations.

Furthermore, we have created a culture within the Group to make it clear that bribery and corruption are completely unacceptable. We protect fundamental human rights by never tolerating the use of underage workers or any type of forced labour. We ensure that our suppliers have the smallest possible impact on the places and the communities in which they work. We will bar any supplier that breaches these standards or is directly or indirectly complicit in such a breach from any further connection with Drax's supply chain.

In 2016, the Group developed *Doing the right thing*, a publicly available document that sets out the principles underpinning our compliance culture. Employees are required to conduct their business in accordance with these principles, in addition to the policies and procedures that comprise our wider compliance framework.

We encourage any employee to speak out in complete confidence through our policy on whistleblowing. This gives them information about how to disclose any information or concerns they may have, in good faith that relate to safety, fraud or other illegal or unethical conduct.

Our tax strategy reflects our understanding of the fact that public policy on taxation and the entire tax environment is changing. In 2016 we paid taxes of more than £130 million. These included taxes on our profits, taxes on our workforce, taxes levied for burning fossil fuels as well as environmental taxes. This figure excludes VAT.

In 2017 we will ensure compliance in full with the requirements of the Modern Slavery Act and a statement will be published on our website as required. We will also comply in full with the new requirements on reporting pay by gender when these are introduced.

SUPPLY CHAIN

Non-fuel procurement

We strive to find working partners and suppliers from a diverse range of backgrounds. Whenever we can we aim to partner with small and medium-sized organisations in the communities where we work.

We are signed up to the Prompt Payment Code and are completely committed to paying our suppliers on time. We fully understand the vital importance of prompt payment to our suppliers' cash flow, particularly for the smaller businesses among them.

We understand that sustainability policy must focus on social, economic and environmental factors as well as price, service and quality. We have adopted these broader principles throughout our procurement practices.

INVESTOR RELATIONS

Drax sees timely and accurate communication with shareholders as central to our relationship. We share results, prospects and our latest thinking with investors through a wide range of channels. These include our Annual General Meeting, our Preliminary and Interim results announcement, our Annual report and accounts and Trading updates. These documents can all be found online at www.drax.com.

We ensure that any important issues that affect our trading and the growth and direction of Drax Group are shared in a timely way through the appropriate regulatory information service, and through our website and social media as soon as is practicable.

We often follow announcements with more detail for our investors through conference calls or presentations. We hold regular meetings with major institutional shareholders along with other potential investors, to help them understand our communications and to enable the Board to gather valuable feedback.

We use the investor section of our website to enable private investors to gain an accessible and transparent understanding of the business and its strategic direction.

PUBLIC AFFAIRS

It is vital to our business that we develop and maintain good relationships with individuals from public life, whether they be elected representatives, appointed officials or key opinion formers.

In 2016, following consultation with our stakeholders, we played a leading role in a number of initiatives, including:

Northern Powerhouse

We met with several of our regional stakeholders, including policy makers and members of our supply chain in the North of England, who said they would like to see Drax take on a more prominent leadership position on the development of the "Northern Powerhouse" concept. Drax also believes the generation of renewable energy, particularly offshore wind and biomass generation, is one of the region's key strengths which the Northern Powerhouse should promote. To help ensure renewable energy has its rightful place at the heart of the Northern Powerhouse and the Government's wider industrial strategy, Drax was delighted to join the Northern Powerhouse Partnership and to pledge its support for the Prime Minister's Northern Powerhouse Partnership Programme.

Energy UK

Drax continues to play an active role in Energy UK, the trade body for the UK's electricity industry. As a member of the Energy UK board and several working committees, Drax is well positioned to take a leading role on the key generation and retail challenges facing the industry as it undergoes a transformation to meet the challenges of a low carbon future. In the past year Drax has worked with Energy UK on important issues including the relationship between heat and electricity policy, transmission network charging reform, how best to deliver cost-effective decarbonisation and enhancing existing market mechanisms that ensure security of supply.

Biomass UK (the Renewable Energy Association's biomass power sector group)

A consistent theme emerging from our stakeholder engagement has been the need to ensure the UK biomass sector is properly represented and that the whole biomass power sector speaks with a unified voice to highlight not only how it ensures the biomass used in power generation is sustainable but also that our messages of the benefits of biomass generation are more widely understood. In particular, few people understand the true value of the flexible, reliable and low carbon power that sustainable wood pellets provide in the UK. Drax was instrumental in the reinvigoration and rebranding of the Biomass Power Sector Group which Drax now chairs and helps support financially.

European Trade Associations: EURELECTRIC and AEBIOM (the European Biomass Association)

The European Commission proposed new sustainability criteria for sold biomass as part of its revision of the Renewable Energy Directive in December 2016. Drax is well known for having some of the most robust biomass sustainability criteria in the world and strongly backs the EU's plans for robust and pragmatic sustainability criteria for solid biomass across the EU. As such, Drax continues to fully engage with the Commission and the other EU Institutions as they draw up the policy. We do so bilaterally and also through the trade associations which represent the power and biomass sectors in Brussels. Drax is now represented on the Board of AEBIOM and chairs EURELECTRIC's taskforce on biomass.

While we are keenly interested in the field of public affairs, we have no interest in party politics. This is why we made no political donations anywhere during 2016 (2015: nil). We are proud to state that we will continue to have contact with people who are active in politics only in order to promote the Group's legitimate business interests.

What counts as political expenditure within the EU encompasses a very wide range of activities, many of which may not be considered as political in a normal sense. In order to avoid breaching EU legislation in any way – entirely unknowingly – Drax presents a resolution at the Annual General Meeting to seek shareholders' approval for expenditure in this area of £100,000 by the Company and its subsidiaries.

Drax Biomass Inc.
Drax Biomass Inc. regularly meets with elected officials and policymakers at the federal state and local levels to advise on business plans, industry developments and policy matters of importance to the business and our suppliers and customers. In addition, Drax Biomass maintains an active presence in state and local business associations to raise the biomass industry's profile within the broader business community, and to advance measures that promote local economic development.

Drax Biomass also engages with the broader forestry sector through memberships in various state forestry associations, including those in Louisiana, Mississippi, Arkansas and Georgia. These associations allow us to work alongside landowners, foresters, state officials and other forest product manufacturers on issues related to conservation, development and responsible use of forestland.

COMMUNITY RELATIONS

In the course of 2016, the Group donated a total of £125,233 to a range of charitable and non-charitable causes in the community. Charitable donations totalled £114,791.

Drax Power Station is a major employer in the Selby area. We also play a positive role in the local community, and support various initiatives at a local and regional level. We do this by giving funding to charities and events by developing and running campaigns in the educational environmental fields. Our nominated charity for 2016 was Selby Hands of Hope, to whom we donated a total of £20,337. We also meet regularly with local officials to ensure we listen to any concerns they may have and to keep them up to date on recent developments and future plans.

Our community engagement reaches wider audiences through seasonal events held at our Skylark Nature Reserve. This year the business has also focused on future employability of young people through our STEM challenge, which engages local school children (ages 11 to 18) in a competition to develop an idea to improve something in their communities. The challenge requires them to apply their science and engineering know-how to come up with an inventive solution, as well as mathematics skills to budget and plan its implementation.

Drax Biomass Inc. conducts local and regional outreach through our participation in sustainability-related certification programmes. For example, in early 2016, Drax Biomass completed an extensive stakeholder consultation with the local communities surrounding our facilities as part of our successful bid to achieve certification under the Sustainable Biomass Program. We contacted over 200 individuals and organisations representing environmental interests, landowners, Government, academia and other stakeholders. We provided them with an overview of our core principles and sourcing practices, and solicited recommendations to strengthen our risk management framework.

In liaising with its local community, Haven employees have been involved in a number of community initiatives throughout 2016, including supporting a local charity transforming woodlands into a tranquil setting for terminally ill people and children with severe learning difficulties; and providing advice at local school recruitment workshops. Various monthly events organised by employees meant that Haven's charity of the year – The Children's Ward at the Ipswich Hospital – was able to benefit from donations in excess of £8,000.

VISITORS TO DRAX

Drax Power Station welcomed over 16,000 people in 2016, an increase of 19% on 2015's figures. This increase is thanks to a more streamlined booking system and more tailored tours, designed to offer visitors the particular areas of interest they want, especially the curriculum-based tours for schools and colleges.

In addition to this, we are now welcoming groups from a more diverse background. With improved use of social media, we are attracting community groups such as Rotary, WI, U3A and special interest groups such as train enthusiasts and engineering specialists.

Tours of the power station have been updated to tell the story of sustainable wood pellets, the upgrade to biomass power, the logistics involved in transporting and storing the pellets, as well as their treatment and use of biomass pellets to produce electricity.

Drax Power Station is now also open on weekends in order to allow family access to the site, enabling people to visit who previously hadn't been able to do so and create a learning environment for the whole family and an exciting experience.

Drax now has the use of two, specially designed, electric buses that can take visitors around the site, quickly and efficiently, with zero emissions on site, adding to the renewable credentials that we talk to the visitors about. These have proven an excellent way of engaging with the visitors as they allow conversations to take place and the visitors to get closer to the plant itself, so they can experience more of the "wow" factor.

GROUP FINANCIAL REVIEW

In a year of significant operational and market challenge, we have performed in line with our guidance.

INTRODUCTION
In 2016 we continued to face a challenging business environment, with sustained weakness in power prices and uncertainty following the UK's decision to leave the European Union in June.

However, whilst Group EBITDA of £140 million is some £29 million lower than in 2015, once the impact of a full year of lost Levy Exemption Certificate (LEC) income is taken into account (circa £30 million), the underlying financial performance of our business was creditable and in line with our guidance. This is a clear indicator of the continued strength in our operations, the resilience of the business and its agility in responding to the challenges faced.

A major feature of our results during 2016 was the impact of Sterling depreciation following the Brexit vote. This led to significant gains in our balance sheet and income statement from unrealised gains on derivative contracts, largely relating to foreign exchange hedges. A gain relating to Sterling depreciation was also recognised within interest charges. In the medium term these changes will be managed through our extensive hedging programme, but in the longer term, without action on our part, Sterling's sustained depreciation may lead to increases to our fuel costs. We are already working on solutions, should this occur.

Furthermore, 2016 was the year we laid the groundwork for future growth, with the final clearance of our Contract for Difference (CfD) in December marking the conclusion of our biomass transformation, the conditional acquisition of Opus Energy, subsequently completed in February 2017, and investment in four Open Cycle Gas Turbine (OCGT) generation opportunities in the UK.

We continue to maintain a robust balance sheet, with net debt of £93 million at 31 December reduced from £187 million in 2015 due to positive cash flows arising from our focus on efficient use of working capital. We will continue to focus on working capital and cash optimisation during 2017 and remain committed to maintaining a strong balance sheet. While the financing of the Opus acquisition will add leverage to our balance sheet, we expect our net debt to be back down to around 2xEBITDA by the end of 2017.

The new strategy the Group has adopted in 2016 is designed to accelerate the development of more long-term sustainable earnings and less dependence on commodity prices. I am increasingly confident that this new strategy, when combined with the Group's critical position in the UK energy system and strong asset base, provides an excellent platform upon which to increase shareholder value.

REVENUE
£2,950M
(2015: £3,065m)

GROSS MARGIN
£376M
(2015: £409m)

EBITDA
£140M
(2015: £169m)

PROFIT AFTER TAX
£194M
(2015: £56m)

BASIC EPS
48PENCE
(2015: 14 pence)

FINANCIAL PERFORMANCE

REVENUE

Consolidated revenue for 2016 of £2,950 million was £115 million lower than in 2015. Electrical output from our Generation business of 19.6TWH was significantly lower than 26.7TWH in 2015, as lower market power prices resulted in our coal-fired units being out of merit for much of the summer.

The impact of lower power prices, and the resultant lower load factors, was somewhat mitigated by a combination of the flexibility and reliability of our generation plant and increased Renewable Obligation Certificate (ROC) revenues, recognised when we sell ROCs to third parties, of £362 million. Our ability to quickly respond to changes in demand, combined with high availability, enabled us to capture real value in the short-term prompt and system balancing markets.

Revenue also includes £47 million in revenues arising from provision of Ancillary Services, an increase of £33 million from 2015. This included a 12-month black start contract signed with National Grid in May 2016, and demonstrated the value of the flexible, reliable support services our generation plant can provide to the UK electricity network.

As described in the Chief Executive's Review the CfD contract for our third unit conversion was approved under State aid rules by the European Commission on 19 December 2016. We commenced generating power under this contract on 21 December and recognised revenue of £10 million in accordance with our accounting policy (set out in further detail in note 2.2 to the financial statements) in the period.

The CfD approval arrived much later in the year than originally anticipated, leading to a financial result at the lower end of market guidance.

Retail power revenues increased from £1,285 million in 2015 to £1,320 million in the year, underpinned by growth in sales to 14.6TWH (2015: 13.8TWH) which reflects strong performance in a highly competitive market.

GROSS MARGIN

Consolidated gross margin for 2016 of £376 million is primarily derived from our generation activities and reflects a creditable performance when considering the loss of income from LECs. This compares to £409 million in 2015.

The prior year included £34 million of income from LECs, earned prior to the cessation of the Climate Change Levy exemption in August 2015. Gross margin performance before LEC income was therefore consistent year-on-year, despite the challenging commodity price environment.

ROCs continue to form an essential component of our financial performance. The expected benefit of ROCs earned is recognised as a reduction in our biomass fuel costs at the point of generation and subsequently recognised as revenue when the ROC is sold to a third party. We earned ROCs reducing costs, with a total value of £536 million in 2016 (2015: £482 million).

We delivered a strong operational performance across our Group, with our Retail and Biomass Supply businesses increasing their gross margin contributions by £4 million and £17 million respectively, driven by increased sales volumes. Further segmental financial performance data is provided in the notes to our consolidated financial statements on page 125.

EBITDA

Operating costs of £236 million were slightly lower than the previous year (2015: £240 million).

Our US-based wood pellet manufacturing business saw an increase in costs reflecting its first full year of commercial operations – with 558 kt of pellets shipped to Drax Power Station compared to 243 kt in 2015.

We incurred costs of £2 million in the delivery of strategic options across the business, including the acquisition of Opus and four OCGT sites (see below). These investments have been offset by operating cost savings delivered from our ongoing focus on cost and value efficiency across our Group. In particular, our Generation business delivered a net saving of £12 million in operating costs compared to 2015, despite a record year for the volume and value of maintenance work completed.

As a result of these costs and the gross margin performance described above, consolidated EBITDA for 2016 was £140 million, compared to £169 million in 2015.

EBIT

Following the completion of our biomass transformation work, combined depreciation charges and losses on the disposal of fixed assets increased from £108 million in 2015 to £113 million in the year.

NET INTEREST CHARGES

Net interest charges of £6 million are very low compared to previous years (2015: £17 million) due to substantial gains on balances held in foreign currencies following the depreciation of sterling in the second half of the year. A full breakdown of the components of interest is shown in note 2.5.

UNREALISED GAINS ON DERIVATIVE CONTRACTS

A key component of the Group's risk management strategy is the use of forward contracts to secure and de-risk the future cash flows of the business.

Whilst these contracts are all entered into for risk management purposes, a proportion of our portfolio is not designated into a hedge accounting relationship under IFRS. Where this is the case, the unrealised gains and losses arising from the change in market value of these contracts is recognised in our income statement.

In 2016, we recognised unrealised gains of £177 million (2015: £124 million) within the income statement, below EBITDA and excluded from underlying earnings, in respect of outstanding contracts for future delivery. In our balance sheet a similar, gain was recognised of £327 million (2015: £23 million) in the hedged reserve.

The gains principally relate to forward foreign currency purchase contracts and reflect the value of our hedge as Sterling has weakened substantially against the US dollar and Euro in 2016, currencies in which the majority of our fuel purchases are denominated.

The term for which we can hedge is limited by available credit lines and market liquidity. Our existing currency hedge extends to 2021, beyond which if markets remain at current levels there is a risk that the cost of our fuel purchases will materially increase.

The accounting treatment of these contracts is set out in further detail in note 7.4 to the consolidated financial statements.

FINANCIAL POSITION

PROFIT BEFORE/AFTER TAX
Profit before tax, in accordance with IFRS, is £197 million for 2016, compared to £59 million for the previous year. The year-on-year change predominantly reflects one-off asset obsolescence charges of £109 million in 2015 and the £53 million increase in unrealised gains due to the increased value of our foreign currency purchase contracts described above.

The tax charge for the year of £3 million (2015: £3 million) is described further below and results in profit after tax of £194 million (2015: £56 million), or basic earnings per share (EPS) of 48 pence (2015: 14 pence).

UNDERLYING PROFIT BEFORE/AFTER TAX ("UNDERLYING EARNINGS")
We also calculate underlying earnings, which excludes the effect of unrealised gains and losses on derivative contracts, to assess the performance of our Group without the income statement volatility introduced by non-cash fair value adjustments on our portfolio of forward commodity and currency purchase contracts.

In addition, in 2016 we have excluded from the underlying earnings the material one-off non-cash credit arising from the recognition of a £31 million deferred tax asset in relation to accumulated start-up losses in our US business. The business has now reached an operational maturity which makes future profitability probable. In 2015, we excluded an asset obsolescence charge of £109 million.

Underlying profit before tax for 2016 of £21 million reduced from £46 million in 2015, reflecting lower EBITDA and higher depreciation charges, partially offset by lower net interest costs.

The underlying tax credit for 2016 of £0 million (2015: £1 million) excludes the tax effect of non-underlying translations.

This results in underlying EPS of 5 pence per share (2015: 11 pence per share).

CAPITAL EXPENDITURE
Capital expenditure of £96 million, reduced from £174 million in 2015, reflects lower biomass transformation spend and ongoing maintenance expenditure in respect of our generating assets partially offset by investment in our US pellet plants.

Total spend on our biomass transformation stands at £673 million. With the generation transformation complete and a small level of residual work to conclude our Industrial Emissions Directive compliance work in 2017 the project has been delivered in line with original cost estimates.

Looking forward, we have assessed the likely future prospects of our existing generation fleet and associated assets and have taken the decision to reduce the expected remaining useful economic life of coal-specific assets to a long stop date of 2025, in line with the Government's stated ambition for the cessation of unabated coal generation. This will result in an acceleration of depreciation up to 2025 and higher depreciation charges of approximately £30 million per annum, from 2017.

We remain confident in the future prospects of our generating assets and stand ready to convert more of our units to run on biomass fuel with the right support. Furthermore, we will invest in our generating units' reliability and flexibility to ensure we can continue to provide the essential services required by the grid and maximise the value of our Generation business. We will continue to invest in optimising our generation and wood pellet manufacturing assets to ensure we can continue to deliver a secure and flexible energy source, and take opportunities to grow the Group's capabilities.

CASH GENERATED FROM OPERATIONS
Cash generated from operations amounted to £213 million in 2016, a £47 million increase from the previous year.

Despite the reduction in profitability year on year our continued focus on efficient working capital and cash management helped to release a further £62 million of cash, principally driven by the acceleration of Retail receivable cash flows following the execution of a new monetisation facility in the first half of the year.

UNDERLYING PROFIT AFTER TAX

£21M

(2015: £46m)

UNDERLYING EPS

5PENCE

(2015: 11 pence)

CASH GENERATED FROM OPERATIONS

£213M

(2015: £166m)

NET DEBT

£93M

(2015: £187m)

OTHER INFORMATION

We also realised a small net cash inflow of £13 million on our ROC and LEC assets (2015: outflow of £86 million) reflecting the value of these assets generated but not yet sold on our balance sheet, which reduced to £257 million (2015: £270 million). Historically, this value has increased as we generated additional ROCs from biomass-fired generation. Cash from ROCs is typically realised several months after the ROC is earned, however, we have optimised our trading activities to monetise a proportion of these assets and accelerate these cash flows which, for the first time, offset this impact. With the conversion of our third unit under a CfD contract from December 2016, the volume of ROCs we generate in future years will reduce with a consequent benefit to our cash flows in 2017.

The overall net cash inflow for the year was £95 million (2015: net outflow of £47 million) and includes capital investments of £93 million (2015: £179 million) and dividend payments of £11 million (2015: £50 million).

NET DEBT AND FUNDING
Net debt at 31 December 2016 was £93 million, compared to £187 million at the end of 2015, reflecting a stable funding platform and the net cash inflow described above.

Our primary funding platform remains consistent with that in the previous year, with £325 million of term loans drawn down. The maturity profile of our loans extends to 2024, with the first repayments due in 2017.

We remain committed to a strong balance sheet and plan to refinance our existing debt as well as our Opus acquisition facility during 2017, while maintaining a rating in the BB range.

Further information about our funding arrangements is included in note 4.3 to the consolidated financial statements, on page 142.

ACQUISITION OF OPUS ENERGY GROUP LIMITED
On 6 December 2016 we announced the proposed acquisition of Opus Energy Group Limited (Opus), a well-established and proven energy retail business serving the SME market, for consideration of £340 million cash.

As a Class 1 transaction, the proposed acquisition was approved by shareholders at a general meeting on 8 February 2017 and concluded on 10 February 2017, with Drax obtaining control of Opus at that date. Opus is expected to deliver enhanced margins to Drax's retail business having experienced consistent mid-single digit operating profit/EBIT margins over the last three financial years.

Financial information on the assets and liabilities acquired, plus an assessment of the impact of the acquisition on our financial statements, is provided in note 5.1 to the consolidated financial statements on page 146.

The acquisition is partly financed by a new short-term debt facility of up to £375 million at which £200 million has been drawn down, repayable by July 2018. The facility is solely for acquisition purposes.

ACQUISITION OF OPEN CYCLE GAS TURBINE DEVELOPMENTS
On 6 December 2016, we also announced the acquisition of four 299 MW OCGT development projects in the UK for initial cash consideration of £18.5 million.

The initial consideration was funded from existing cash reserves. Assuming full development, the total investment in each project is expected to be in the range of £80–100 million with the timing of this investment dependent upon the timing of associated capacity market contracts.

The net assets acquired as part of this acquisition had a fair value of £22 million. Full details of the impact of the acquisition on our financial statements is included in note 5.1 to the consolidated financial statements on page 146.

TAXATION
The 2016 tax charge of £3 million compares to £3 million in 2015. In 2016, the one-off non-cash deferred tax credits arising from the reduction of future UK corporation tax rates to 17% from 2021 (£12 million) and the recognition of deferred tax assets associated with start-up losses in our US business for which we consider the associated future tax benefit to be probable (£31 million) reduced the overall tax charge.

The underlying effective rate of tax (excluding the post-tax impact of unrealised gains on derivatives contracts and US deferred tax) is -10%, less than the standard rate of corporation tax in the UK, the difference arising predominantly from the impact of the corporation tax rate changes described above. The comparable underlying rate in 2015, which in addition excluded the post-tax impact of asset obsolescence charges, was -4% and also included the impact of future corporation tax rate changes announced in the 2015 Budget.

Cash taxes paid during the year were £2 million (2015: £6 million).

DISTRIBUTIONS
The Board has begun a review of our dividend policy, but for 2016 our policy remains to distribute 50% of underlying earnings in each year. Underlying earnings for the year ended 31 December 2016 were £21 million (2015: £46 million), as described above.

On 22 February 2016, the Board resolved, subject to approval by shareholders at the Annual General Meeting (AGM) on 20 April 2016, to pay a final dividend for the year ended 31 December 2015 of 0.6 pence per share (£2.4 million). The final dividend was subsequently paid on 13 May 2016.

On 25 July 2016, the Board resolved to pay an interim dividend for the six months ending 30 June 2016 of 2.1 pence per share (£8.6 million), representing 50% of underlying earnings for the period. The interim dividend was paid on 7 October 2016.

At the forthcoming AGM, the Board will recommend to shareholders that a resolution is passed to approve payment of a final dividend for the year ended 31 December 2016 of 0.4 pence per share (£1.8 million), payable on or before 12 May 2017.

Shares will be marked ex-dividend on 20 April 2017.

VIABILITY STATEMENT

STATEMENT OF VIABILITY
In accordance with provision C.2.2 of the 2014 version of the UK Corporate Governance Code, the directors have assessed the prospects of the Group over a period significantly longer than the 12 months required by the going concern provision.

In preparing this assessment of viability the Board has considered the principal risks faced by the Group, relevant financial forecasts and sensitivities, the availability of adequate funding and the strength of the Group's control environment.

ASSESSMENT PERIOD
The Board conducted this assessment over a period of three years, which was selected for the following reasons:

- The Group's Business Plan, which is reviewed and assessed on a quarterly basis and is used for strategic decision making, includes a range of financial forecasts and associated sensitivity analysis. This Plan covers a three-year period in detail.
- Within the three-year period liquid commodity market curves and established contract positions are used in the forecasts. Liquid curves typically cover a one to two-year window and contracts cover periods between one and ten years. In particular, we benefit from the stable and material earnings stream available from the CfD until 2027. Selecting a three-year period balances short-term market liquidity against our longer term contractual positions.
- Within a three-year horizon there is limited certainty around markets and regulatory regimes. However, in selecting this period the Board has assumed no material changes to the Group's mid-term regulatory environment and associated support regimes.

REVIEW OF PRINCIPAL RISKS
The Group's principal risks and uncertainties, set out in detail on pages 55 to 61, have been considered over the period.

The principal risks with the potential to exert significant influence on viability are: commodity price changes, political and regulatory changes, biomass acceptability changes and plant operating failures. A significant adverse change to the status of each risk has the potential to place material financial stress on the Group.

The risks have been evaluated, where possible, to assess the potential impact of each on the viability of the Group, should that risk arise in its unmitigated form. The potential inputs have been included, where appropriate, as sensitivities to the Plan and considered by the Board as part of the approval process required before the Plan is adopted by the Group.

REVIEW OF FINANCIAL FORECASTS
The Plan considers the Group's financial position, performance, cash flows, covenant compliance and other key financial ratios over the period and was most recently updated to reflect current market and environment conditions in December 2016.

In addition, the Plan considers the financial impact of the Opus acquisition and the implications for the earnings, cash flows and working capital position of the Group.

The Plan includes certain assumptions, the most material of which relate to commodity market price curves and levels of subsidy support available to the Group through the generation of biomass-backed renewable power.

The Plan is subject to stress testing, which involves the construction of reasonably foreseeable scenarios, including those aligned to the principal risks, which test the robustness of the Plan when key variables are flexed both individually and in unison. Where such a scenario suggests a risk to viability, the availability and quantum of mitigating actions is considered.

The Board considers the most significant of these scenarios in the assessment period to be a significant deterioration of commodity market prices, leading to a fall in the available price for power and thus a fall in the margins available to the Group from its power generation activities. This has been considered in the Plan and the Board is satisfied that in such a scenario sufficient actions could be taken to preserve the viability of the Group.

AVAILABILITY OF ADEQUATE FUNDING
The sources of funding available to the Group are set out in note 4.3 to the consolidated financial statements (see page 142). The Board expects these sources, along with cash flows generated by the Group from its normal operations, to provide adequate levels of funding to support the execution of the Group's Plan.

The £375 million loan facility entered during February 2017 to finance the Opus acquisition matures during July 2018 and the debt drawn will therefore need to be refinanced or renewed during the three-year period. As reported on page 142 a full review of the Group's sources of funding is now underway and the Board remains confident that this will result in adequate funding being available beyond the viability horizon.

EXPECTATIONS
The directors have considered all the factors in their assessment of viability over the next three years, including the latest Plan, scenario analysis, levels of funding, control environment and the principal risks and uncertainties facing the Group. The directors have also considered the availability of actions within their control in the event of plausible negative scenarios occurring. They have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three-year period of their assessment.

PRINCIPAL RISKS AND UNCERTAINTIES

The Board is responsible for defining risk appetite and ensuring the effectiveness of risk management and internal controls across the Group. The Group has a comprehensive system of governance controls to manage key risks.

GROUP APPROACH TO RISK MANAGEMENT

The Group has a Risk Management Policy in place, approved by the Board which defines the Group's approach to risk management. The key elements of the Policy are as follows:

- identify principal risks that threaten the achievement of our strategic objectives then assess their significance to the business;
- put in place appropriate mitigating controls to manage identified risks to an acceptable level;
- escalate and report principal risk and control information to support management decision making;
- assign responsibility and define accountabilities for risk management and put these into practice across the Group;
- continuously monitor the changing risk environment, the Group's principal risks, the effectiveness of mitigation strategies and the application of the risk framework.

The approach manages rather than eliminates the risk of failure to achieve business objectives, and provides reasonable, not absolute, assurance against material misstatement or loss.

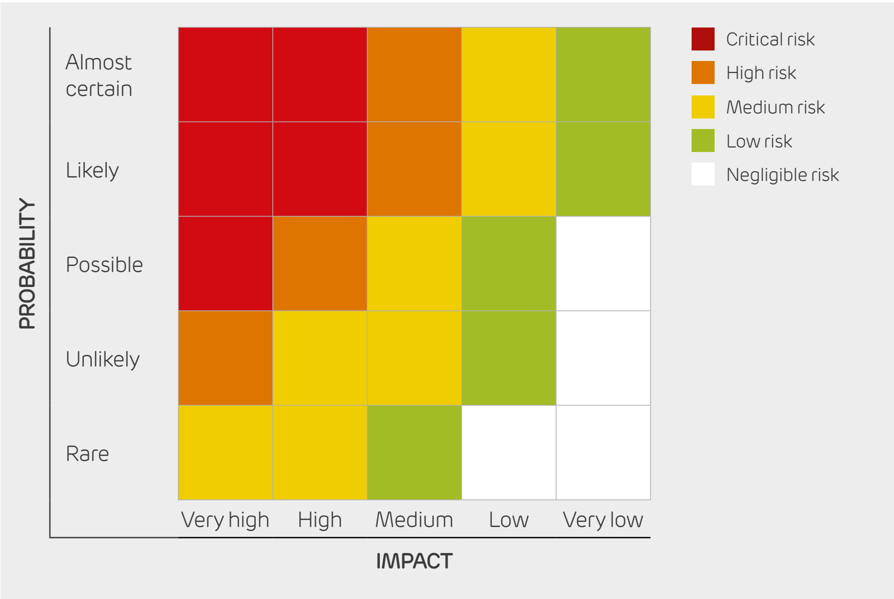
The risk management governance structure includes seven business risk management committees (RMCs).

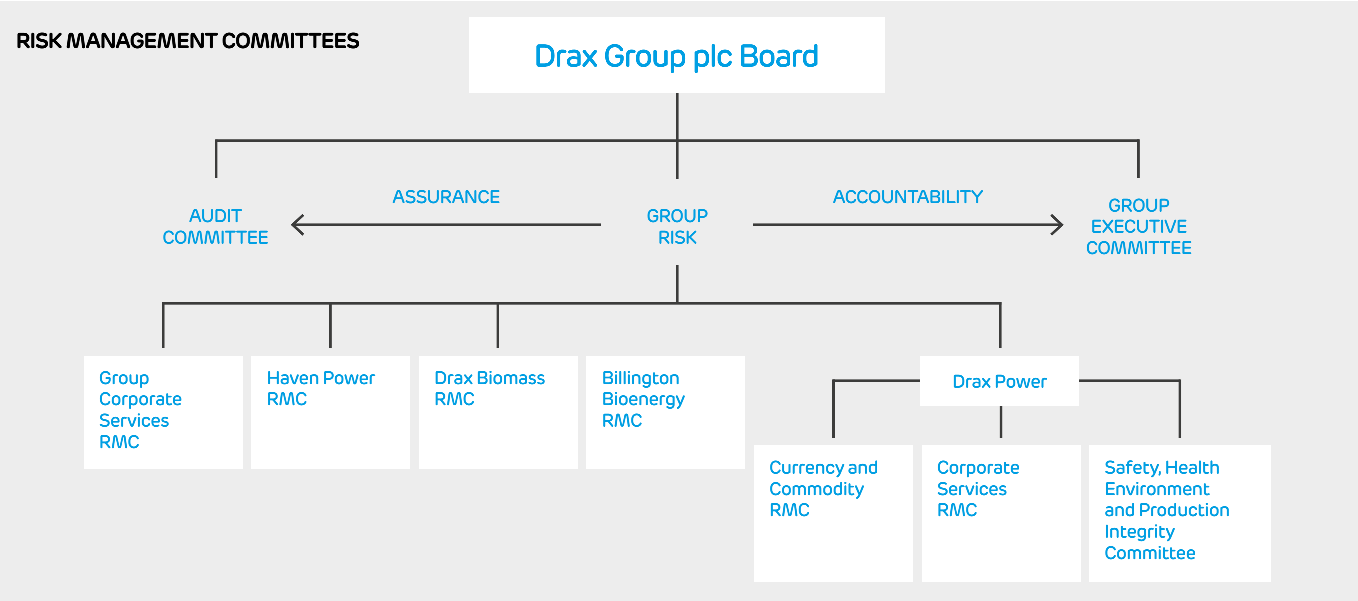
Each RMC reports to the executive management of that area, assisting in the management of their risks. In turn, each executive is responsible for their risks to the Group Executive Committee.

Each RMC is responsible for ensuring that all risks associated with its specific area of the business are identified, analysed and managed systematically and appropriately. Each RMC has terms of reference that require local level risk policies and control systems to be approved, implemented and monitored in order to ensure that activities are commensurate with the risk appetite established by the Board, are adequately resourced and comply with applicable legal and regulatory requirements. Each RMC reports to the Board annually on the management of risks within the scope of its responsibilities.

RMCs review new and emerging risks and changes to existing risks. A top down review of risks is performed by each RMC and by the Group Executive Committee on at least an annual basis. New risks are also identified during development of the Business Plan.

A new Group risk scoring matrix has been adopted in 2016 to align scoring across all RMCs. Risks are scored based on impact and probability as follows:





The Group Executive Committee and the Board review reporting on critical and high risks from each RMC at least annually and from Group Risk biannually. In addition, the Audit Committee reviews the suitability and effectiveness of risk management processes and controls on behalf of the Board.

INTERNAL CONTROL

The Group has a comprehensive and well-defined internal control system with clear structures, delegated authority levels and accountability. The Board has adopted a Schedule of Matters which are required to be brought to it for decision. The internal control system is designed to ensure that the directors maintain full and effective control over all significant strategic, financial and organisational issues.

Through the Audit Committee, the Board has implemented a programme of internal audits of different aspects of the Group's activities. The programme is developed based on an assessment of the key risks of the Group, the existing assurance and controls in place to manage the risks and to the core financial control framework.

The results of each internal audit are documented in a report for internal distribution and action. A full copy of the report is distributed to the Group Executive Committee and the Chair of the Audit Committee, with an executive summary going to the other members of the Audit Committee. Each report includes management responses to Internal Audit's findings and recommendations and an agreement of the actions that management will take to improve the risk management and the internal control framework. In addition to the results of work undertaken by Internal Audit, the Audit Committee also satisfies itself that an action plan is in place and management are addressing issues raised by the external auditor in their yearly management letter.

Based on the reporting from the RMCs and from the Audit Committee in 2016, the Board determined that it was not aware of any significant deficiency or material weakness in the system of internal control.

CHANGE IN RISK PROFILE

Risks are reported to the Board and disclosed in the annual report and accounts under eight principal risk headings. This has increased from five principal risks disclosed in 2015.

- Information Systems and Security risks have been included in their own right in 2016, rather than being combined under a Corporate risk heading as in 2015. Corporate Risk has been removed.
- Environment, Health and Safety risk has been separated out from Plant Operating Risk.
- Delivery of our Growth Strategy has been added to reflect the adoption of the Group's new growth strategy and the focus of senior management on ensuring its successful implementation.
- Whilst People risk has always existed for the Group, it is now a principal risk as there is increased reliance on key staff due to the pace of strategic change.

1. Strategic risks

Context	Mitigations	Movement	Changes in factors impacting risk in 2016	Strategic priorities
Context The Group has adopted a new policy designed to reduce the exposure to commodity price movements and strengthen the long-term future of the Group. The strategy includes acquisitions and expansion into new activities with their associated risks. **Risk and impact** – The benefits from our strategy may not be realised fully if we do not integrate Opus effectively. – Development of the four OCGT plants is dependent on winning contracts in capacity market auctions which is not certain. – The markets where we operate and are looking to grow are constantly evolving, making the identification and implementation of further opportunities for growth more challenging.	– A rigorous programme management framework has been established to drive successful integration of Opus. – Significant development costs for the OCGT plants will only be incurred if a contract is won in a capacity market auction. – We continually analyse the changing dynamics of the markets in which we operate. – A programme of research and development into new technologies, products and markets has been established.	^	– A new purpose and strategy and the acquisition of Opus and four OCGT development projects. – We are actively pursuing potential acquisitions of pellet plant facilities.	Targeted long-term growth

2. Political and regulatory risks

Context / Risk and impact	Mitigations	Movement	Changes in factors impacting risk in 2016	Strategic priorities
Context We remain vulnerable to changes in Government policy. The energy sector is subject to detailed legislation and regulation that is frequently changing and ever more stringent. **Risk and impact** – Changes to UK policy and regulations may reduce our ability to deliver our forecast earnings from our base business and our growth strategy, putting pressure on our financial results and cash flows. – More complex and challenging regulations could lead to non-compliance.	– Engagement with politicians across the political spectrum and Government officials to influence thinking. – Communication of our socio-economic value to the UK. – Working with think tanks and specialist consultants to establish Drax as a thought leader on priority policy and regulatory issues. – Engagement with regulators to ensure compliance with regulatory requirements. – Working with Energy UK to develop voluntary codes of practice in retail.	›	– The Government has confirmed that biomass conversions will not be eligible to participate in the 2017 CfD auction. – The Government has confirmed the Carbon Price Floor will remain unchanged at its current level until 2020/21. – Government has issued a consultation on the closure of all coal stations in the UK by 2025. – Brexit has created uncertainty over UK participation in, and influence over, discussions on new EU legislation – The growing importance of principles-based regulation in the retail sector was emphasised by Ofgem's plans to extend the scope of principles in the supply licence, and by significant penalties on suppliers for failures under the standards and conduct principle. – There has been an increase in the momentum of the smart meter roll-out. Ofgem has been consistent on the importance of achieving the roll-out timetable and has fined one company for failures under the related advanced meter programme. – The obligation from the CMA enquiry on improving customer engagement and competition, to disclose prices of all acquisition and retention contracts for microbusinesses, will result in increased costs.	Higher Quality Diversified Earnings Operational Excellence

3. Biomass acceptability risks

Context
The biomass market is still relatively new, sustainability legislation at both an EU and UK level is evolving, and public understanding of the benefits of the technology needs to be improved.

Risk and impact
- EU or UK sustainability policy changes could be excessively onerous and make it difficult for us to comply with policy requirements and claim subsidy in support of economic biomass generation.
- Detractors and some eNGOs have been known to act in concert to try and influence policymakers against wider biomass use and future biomass conversions, which could make it difficult to gain support for further conversions.

Mitigations
- Increased engagement across all European Institutions (Commission, Parliament, Council), and relevant UK Government departments.
- Strong coalition with other utilities and those engaged in forest industries including using EU and US forestry expertise to brief Brussels.
- Increased transparency in how we evidence sustainability.
- Working with academics, think tanks and specialist consultants to improve understanding and analysis of the benefits of biomass.
- Engagement with key NGOs to discuss issues of contention.
- Media, including social media, presence to respond in the public domain to eNGOs.

Movement

Changes in factors impacting risk in 2016
- UK sustainability standards became mandatory in December 2015 and we have demonstrated full compliance to date
- The European Commission has published its draft biomass sustainability criteria as part of the new Renewable Energy Directive (so called Winter Package), following extensive consultation. The proposal includes substantial elements similar to the UK's existing sustainability regime but is still subject to Council and Parliament scrutiny and negotiation.

Strategic priorities
Higher Quality Diversified Earnings

Operational Excellence

4. Plant operating risks

Context
The reliability of our operating plant is central to our ability to create value for the Group.

Risk and impact
- Single point failures of plant could result in forced outages in our generation or pellet production plants.
- Changes in generation running regimes expose us to new and emerging technical risks which could result in higher than forecast forced outage levels.
- Successful generation using biomass requires stringent quality throughout the supply chain, which continues to evolve and mature. Poor quality could result in unplanned loss of generation.

Mitigations
- Comprehensive risk-based plant investment and maintenance programme.
- Adequate insurance in place to cover losses from plant failure where possible.
- Significant research and development on the production of wood pellets as well as the handling and burning of biomass.
- Full testing of all biomass supplies prior to acceptance and the use of contractual rights to reject out of specification cargoes.
- Stringent safety procedures in place for handling biomass and dust management.
- Increased sampling and analysis through the supply chain to increase understanding of causes of fuel quality issues.

Movement

Changes in factors impacting risk in 2016
- The increase in intermittent generation has led to a reduction in transmission system stability and a more volatile pattern of running for our units, principally the coal units, which places additional thermal stress on the units.
- Lack of demand in the biomass market is putting suppliers under price pressure which in turn could compromise pellet quality as suppliers look to reduce production costs.

Strategic priorities
Operational Excellence

5. Trading and commodity risks

Context

The margins of our generation and retail businesses are influenced by commodity market movements, which are inherently volatile.

Risk and impact

- Fluctuations in commodity prices, particularly gas and power, could result in lower margins and a reduction in cash flow in our generation business.
- Drax Power may fail to secure future grid system services contracts which are a source of revenue diversity for the Group.
- Following Brexit, foreign exchange rates have moved adversely against the pound sterling, which could result in higher costs on unhedged exposures in the mid-term.
- The value of ROCs generated may be lower than forecast if the recycle value outturns below BEIS' projections due to higher than anticipated renewable generation.

Mitigations

- High levels of forward power sales for 2017.
- Hedging retail commodity price exposures when fixed price sales are executed with third parties.
- Wood pellets purchased under long-term contracts with fixed pricing.
- Significant forward foreign exchange hedging in place.

Movement

Changes in factors impacting risk in 2016

- Low power prices and more intermittent generation have reduced economic off-peak running, especially for coal-fired generation.
- Prices for wood pellets were depressed in 2016 due to oversupply in the market.
- Sterling exchange rates against the euro and dollar have experienced significant adverse movements since Brexit and remain weak.
- Low Recycle Fund outturn for 2015/16 RO compliance year as ROC production exceeded BEIS estimates.

Strategic priorities

Management of Commodity Market Exposure

6. Information systems and security risks

Context

The availability, integrity and security of our IT systems and company data are essential to support operations of the Group.

Risk and impact

- Non-availability of IT systems, or a breach in their security, could result in the inability to operate systems or our information could be compromised.
- If our IT architecture does not meet the increasingly demanding and complex requirements of the Group, we may not deliver our growth plans effectively.

Mitigations

- Business continuity, disaster recovery and crisis management plans in place across the Group.
- Cyber security measures, including a defence, detect, remedy strategy, in place.
- IT transformation programme in place to deliver upgraded architecture.

Movement

Changes in factors impacting risk in 2016

- Significant investment in our critical IT systems has improved the general resilience of the core systems.
- Development of the IT transformation programme which is now being implemented.

Strategic priorities

Operational Excellence

7. People risks

Context	Mitigations	Movement	Changes in factors impacting risk in 2016	Strategic priorities
We need to ensure we have the right people in place with the leadership and specialist skills to help the Group to compete, innovate and grow. **Risk and impact** – Our performance and the delivery of our strategy is dependent upon having strong, high-quality leaders and engaged and talented people at all levels of the organisation.	– Retention and talent development strategies in place. – Regular staff surveys to monitor engagement levels and alignment of people with Group values. – Career management programme. – Regular staff communications.		– Development of the new strategy HR identified areas across the Group that will require strengthening as the strategy is executed.	Operational Excellence

8. Environment, health and safety risks

Context	Mitigations	Movement	Changes in factors impacting risk in 2016	Strategic priorities
The health and safety risks of the environment in which we operate make our strong standards and culture crucially important. **Risk and impact** – The health and safety environment is subject to numerous and evolving health, safety and environmental laws, regulations and standards. If we do not operate safely and comply with regulations the wellbeing and satisfaction of our workforce and levels of outage could be adversely affected.	– Well embedded health and safety systems based on world leading systems – Continuous review of health and safety systems particularly as we increase our experience and operating knowledge of handling and burning biomass.		– World class personal safety performance for the year with TRIR well above the industry benchmark. – No legislative changes in the year.	Operational Excellence

Strategic report

The Strategic report is set out on pages 1–61 of this document and was approved by the Board of directors on 15 February 2017.

Dorothy Thompson
Chief Executive, Drax Group

Will Gardiner
Chief Financial Officer

CORPORATE GOVERNANCE

LETTER FROM THE CHAIRMAN

First-class governance along with first-class management remain key to delivering Drax's new strategy of creating sustainable value across the Group's activities.

Dear Shareholder

I am delighted to have completed my first full year as Chairman of the Board of your Company during 2016, and to be making my report on governance during that period.

Directorate changes

The past year has been an important year of change in the Board. Andy Koss, Chief Executive of Drax Power – our power generation business – was appointed to the Board on 1 January 2016, and Will Gardiner who was appointed Chief Financial Officer in November 2015, has completed his first full year of Board membership.

I am delighted to say that both Will and Andy have made a strong, dynamic and positive contribution to the Company's leadership in 2016, along with playing a significant role in the development of our new strategy.

Lastly, Melanie Gee resigned from the Board following the Annual General Meeting (AGM) in April 2016. I thank her once again for the many valuable contributions she made during her three years as a director.

Non-executive directors

The UK Corporate Governance Code (the Code) sees one of the significant roles of non-executive directors as providing "constructive challenge and help in developing proposals on strategy".

In this regard, one of the important elements of my role as Chairman is to ensure that the Board benefits from the skills and experience of non-executive directors who can strengthen its ability to deliver the leadership that your Company needs.

We therefore seek to appoint forward-looking non-executive directors from a diverse range of relevant backgrounds, who can bring experience and good judgement to the Board discussions. To complement and widen our non-executive skills, we will look to recruit two non-executive directors in 2017 who can support the Board.

We also continue to work hard to ensure that the Board is diverse in its widest sense, including gender diversity. Currently, 14% of your directors are female. This will remain one of the factors that the Board takes into consideration in making appointments in the future.

Succession planning and diversity

Maintaining and improving the effectiveness of the Group's succession planning process will be key to the success of the business in the future. Selecting and supporting the right individuals to lead the delivery of the Group's new strategy, together with ensuring that the Board is constantly refreshed, are essential parts of this process.

The Board and I are confident that many of our future leaders are already working within the Group. That is one of the reasons why during 2017, in order to ensure that we identify and support our next generation of leaders, we will be implementing a new people strategy.

Along with the continued work of the Nominations Committee, this will help us to make the most of our "human capital" and continue to create opportunities for talented individuals with the right skills to take the Company forward over the years to come.

The current Board is performing strongly, and has the right expertise and experience to provide excellent leadership. However, as our new strategy comes into place and the Group grows, we may find that we need new skills.

The Board and I are completely committed to ensuring that the Group has access to the brightest talents and the best leaders to deliver our strategy, whether those individuals come from within the Drax "family" or outside. One of the ways we ensure this happens is through linking the leadership team who helped develop the new strategy directly to the senior executives responsible for its day-to-day delivery.

The UK Corporate Governance Code and governance at Drax

Drax reports against the 2014 version of the Code. In 2016, we ran a tender process for the appointment of auditors as discussed in the Annual Report and Accounts 2015. I am pleased to inform you that we were fully compliant with all of the Code's provisions through the entire period of the reporting year and until the date of approval of this report.

As well as ensuring that we maintain the correct blend of skills and knowledge on the Board, we also continue to strive to improve the way we work together to overcome the challenges the business faces, and to develop and deliver strategies for future success.

This means that we are constantly reviewing our governance structures and processes to ensure that they are fit for purpose, and that good governance remains at the heart of the Group. This is not only about doing "the right thing", but also about doing it "the right way". Over a number of years, we have established a strong set of values within the Group. We express these as the acronym "HEAT", standing for honest, energised, achieving and together. They provide a clear behavioural and ethical compass for everyone within the Group in our daily working lives.

The following section concerns the structure and processes that support our corporate governance and the ways in which they have operated during the year ended 31 December 2016.

My role as Chairman

As Chairman, my brief is to make sure that your Company always has a Board which works effectively, efficiently and collectively under my leadership. One key part in achieving this is ensuring that the Board benefits from the right dynamics and good, open communication.

This depends on every director playing his or her part to contribute fully to discussions and debates, and to provide constructive challenge to their colleagues. Thanks to the diverse range of expertise and experience represented on our Board, I am pleased to report that it is functioning very effectively.

The relationship between Chairman and Chief Executive is crucial for the successful management of any company. In my role as Chairman, I speak frequently with Dorothy Thompson, our Group Chief Executive. We regularly discuss the issues being dealt with by the executive team, and any that need to be discussed by the Board. I set the agenda for the Board, and make sure that sufficient time is allowed to cover any matters we need to consider – including the discussion, formulation and execution of strategy.

It is also part of my remit to understand how shareholders view the performance of the business. The Group Chief Executive, the Chief Financial Officer and our brokers keep the Board very closely appraised of shareholders' views. In addition, I do personally engage with shareholders whenever I, the Board, or individual shareholders feel this would be helpful.

Board and committee evaluation

In order to continue to make the Board more effective, I commissioned in 2016 an externally facilitated evaluation of the performance of the Board and its committees. This will help ensure that the Company is even better placed to meet the challenges it will face in the years to come. You can find details of this process and its conclusions in the report of the Nominations Committee on page 74. One of its conclusions was for the Board to invite advisers and external experts to selectively attend Board meetings to share their perspective on the business and the markets in which we operate.

Key areas of focus

Following the completion of our project to become a predominantly biomass-fuelled generator, and the approval of our Contract for Difference (CfD), the Board in 2016 was firmly focused on developing a new corporate strategy designed to deliver success for the long-term.

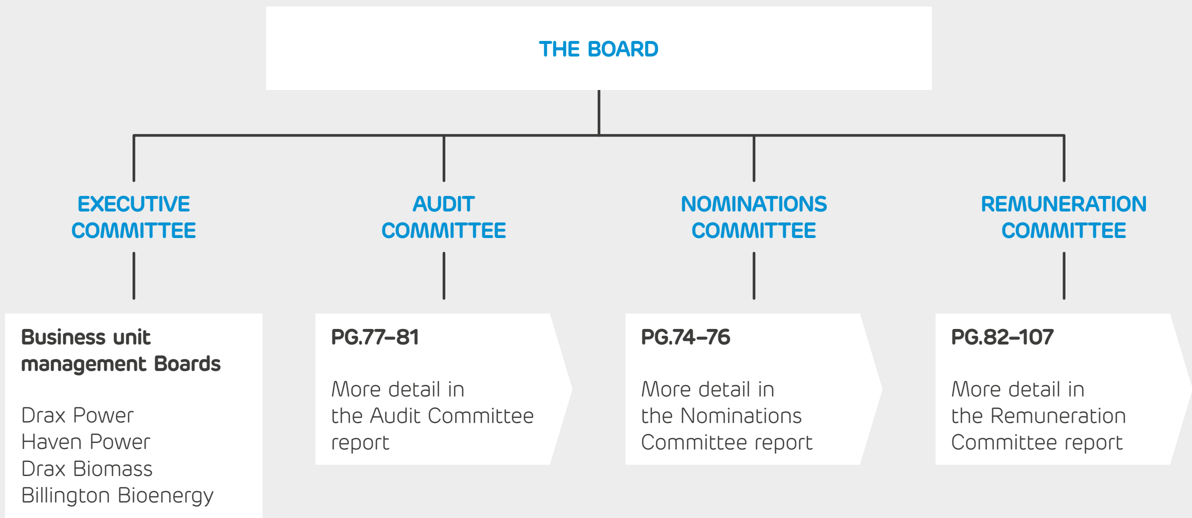
At the heart of this strategy is the creation of a long-term, higher quality, diversified earnings base, strongly linked to the Company's continued commitment to a lower-carbon future for UK energy. The Board identified two major opportunities to realise that strategy in 2016. The first, the acquisition of Opus Energy (Opus), gives us access to a successful, established and profitable retail trading base providing electricity and gas to small to medium-sized businesses across the UK, which will complement our existing offering through Haven Power (Haven). The second comprises four projects to build rapid-response Open Cycle Gas Turbines (OCGT) on sites in England and Wales, providing the flexible supply of electricity that the growth of intermittent renewables requires, ensuring that the UK system remains stable. As ever, we will remain committed to advocating the benefits of sustainable biomass in the shape of compressed wood pellets.

After a full year in post, I am even more confident that Drax Group has the right team in place to lead today, and is identifying the talented men and women who will lead tomorrow.

Philip Cox CBE
Chairman

THE BOARD AND ITS COMMITTEES

OUR GOVERNANCE FRAMEWORK



Role of the Board

The Board determines: the Group's strategy; the Group's appetite for risk; the risk management policies; the annual plan and key performance indicators; acquisitions and disposals and other transactions outside delegated limits; material changes to accounting policies or practices; significant financial decisions; capital structure and dividend policy; shareholder communications; prosecution, defence or settlement of material litigation; Group remuneration policy; the terms of reference of Board committees; and the Board structure, composition and succession.

Terms of reference

The Board has a schedule of matters reserved for its decisions and formal terms of reference for its committees. These are reviewed annually and are available to view on the Group's website at www.drax.com.

Matters which are not specifically reserved to the Board and its committees under their terms of reference, or to shareholders in General Meeting, are delegated to the Executive Committee or otherwise delegated in accordance with a schedule of delegated authorities approved by the Board.

How the Board functions

The Board receives regular reports on performance against the Business Plan and periodic business reports from senior management. It also receives industry, regulatory and topical updates from external experts and advisers, from time to time. Papers are distributed in advance of Board and committee meetings, to brief directors.

Directors may, in the furtherance of their duties, seek independent professional advice at the Company's expense. During 2016, no director sought independent professional advice.

The Company Secretary advises the Board on all governance matters, ensuring good information flows within the Board, its committees, the Executive Committee and senior management. He ensures that Board processes are complied with and is also responsible for compliance with the Listing, Prospectus, Disclosure and Transparency Rules and the Companies Act.

The Company's Articles of Association (the Articles) give the directors power to authorise conflicts of interest. The Board has an effective procedure to identify potential conflicts of interest, consider them for authorisation and record them. The Articles also allow the Board to exercise voting rights in Group companies without restriction (for example to appoint a director to a Group company without this counting as a conflict requiring authorisation).

The Company has appropriate insurance cover in place in respect of legal action against directors of the Company and its subsidiaries.

The Nominations Committee report contains details of the selection, appointment, review and re-election of directors, as well as the Board performance review and directors' development.

Board composition

All of the directors listed on page 65 served throughout the year. Melanie Gee served as a director until her retirement on 20 April 2016. Each of those listed, except for Melanie Gee, remained directors as at the date of the approval of this report. Biographical details of the directors appear on pages 68–70.

THE BOARD IN 2016

Directors
Philip Cox CBE (Chairman)
Tim Cobbold (Independent non-executive director)
Will Gardiner (Chief Financial Officer)
Andy Koss (Chief Executive, Drax Power)
Melanie Gee (retired as a director on 20 April 2016)
David Lindsell (Senior independent non-executive director)
Dorothy Thompson CBE (Group Chief Executive)
Tony Thorne (Independent non-executive director)

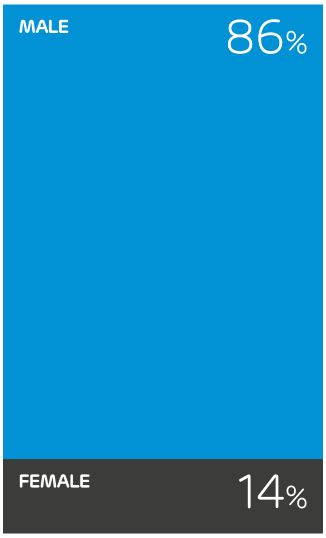
The Group Company Secretary acts as Secretary to the Board.

Board diversity
As at 31 December 2016, there were six male directors and one female director on the Board.

Number of meetings held
- The Board has eight scheduled meetings each year.
- In 2016, an additional six meetings were held by telephone to address matters requiring formal decisions.
- In addition, the Board meets at least annually to consider strategy.

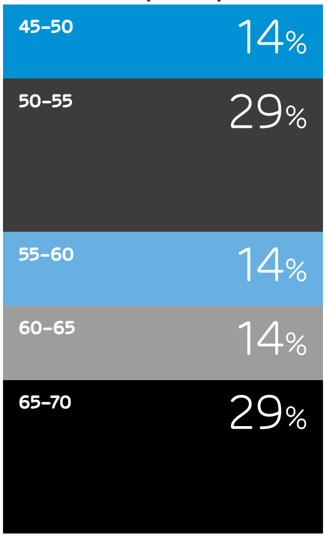
AS AT 31 DECEMBER 2016

DIVERSITY

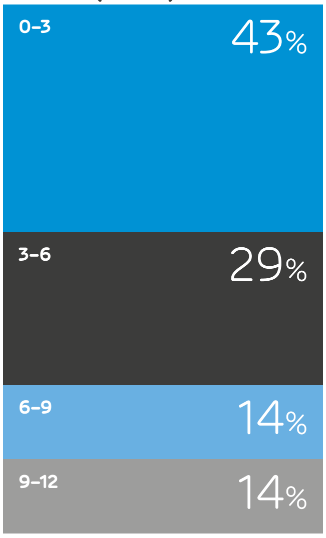


COMPOSITION

AGE PROFILE (YEARS)



TENURE (YEARS)



Board attendance 2016
The table below shows the number of meetings and the directors' attendance during 2016.

	Date appointed as a director and member of the Board	Maximum possible meetings[1]	Number of meetings attended	% of meetings attended
Tim Cobbold	27 September 2010	8	8	100%
Philip Cox	1 January 2015	8	8	100%
Will Gardiner	16 November 2015	8	8	100%
Andy Koss	1 January 2016	8	8	100%
Melanie Gee (retired as a director on 20 April 2016)	1 January 2013	3	3	100%
David Lindsell	1 December 2008	8	8	100%
Dorothy Thompson	20 October 2005	8	7	88%
Tony Thorne	29 June 2010	8	8	100%

Note:
(1) The maximum number of meetings that each individual was entitled to and had the opportunity to attend.

Committees of the Board in 2016

The table below details the standing committees established by the Board and their membership:

	Audit Committee	Nominations Committee	Remuneration Committee	Executive Committee(1)
Tim Cobbold	Member	Member	Member	–
Philip Cox	Invited to attend	Chairman	Member	–
Will Gardiner	Invited to attend	–	–	Member
Andy Koss	–	–	–	Member
Melanie Gee (retired as a director on 20 April 2016)	Member	Member	Member	–
David McCallum(2)	Secretary	Secretary	Secretary	Secretary
David Lindsell	Chairman	Member	Member	
Dorothy Thompson	Invited to attend	Invited to attend	Invited to attend	Chairman
Tony Thorne	Member	Member	Chairman	–

Notes:
(1) The Executive Committee is responsible for the day-to-day management of the Group. In addition to those named above, Pete Madden (President and Chief Executive, Drax Biomass), Matthew Rivers (Director of Corporate Affairs), Peter Bennell (Chief Executive, Haven Power) until 1 September and Jonathan Kini (Chief Executive, Drax Retail) from 1 September, were also members in 2016.
(2) David McCallum is the Group Company Secretary (appointed 1 July 2016).

Details of the work of the Nominations, Audit and Remuneration Committees are given in their respective reports on pages 74 to 107. The committees' terms of reference are reviewed annually by each committee and then by the Board and are available on the Group's website at www.drax.com.

Time commitment

Under the terms of his letter of appointment, the Chairman is expected to commit between 50 and 70 full days a year to this role.

Under the non-executive directors' letters of appointment, each is expected to commit 12 to 15 full days a year. That includes attendance at Board meetings, the AGM, one annual Board strategy day and at least one site visit per year. In addition, they are expected to devote appropriate preparation time ahead of each meeting. The time commitment expected in respect of their membership of the Audit, Nominations and Remuneration committees, is an additional three to four full days a year in each case. Non-executive directors also spend time with management, to maintain their knowledge of the developing business and to understand the operational challenges being faced.

Corporate governance

The Group is committed to high standards of corporate governance, details of which are given in this report.

The various sections of this report summarise certain provisions of the Company's Articles and the Companies Act 2006. The relevant provisions of the Articles or the Companies Act should be consulted if further information is required.

Compliance with the UK Corporate Governance Code

It is the Board's view that throughout the period commencing on 1 January 2016, the Company has complied in full with the principles of the Code issued in September 2014. In respect of the requirement to put the external audit out to tender, a tender process for the external audit took place during 2016 and as a result of this process, Deloitte LLP was reappointed as external auditor for the 2017 financial statements.

Directors' interests, indemnity arrangements and other significant agreements

Other than a service contract between the executive directors and a Group company, or as noted in the Remuneration Committee report, no director had a material interest at any time during the year in any significant contract with the Company or any of its subsidiary undertakings.

There are no agreements between the Group and its directors providing for compensation for loss of office or employment because of a takeover bid.

The Board has reviewed the independence of each non-executive director. None of the non-executive directors who served during the year had any material business or other relationship with the Group, and there were no other matters that were likely to affect their independence of character and judgement. The Board therefore considers all of the non-executive directors to be independent, in accordance with Code provision B.1.1.

Relations with key stakeholder groups

Communication with all our stakeholders is an essential part of our business. Details of communications with our stakeholders are contained in the Stakeholder engagement section of this report beginning on page 46, with further details of our communications with investors set out below.

The Chairman is keen to ensure that he maintains an open relationship with the Company's major shareholders, communicates directly with them and offers them the opportunity to meet any other directors. This enables the Board to understand their views on the Group and its governance.

The Board also reviews and discusses the investor feedback from post-results investor meetings conducted by the Group Chief Executive and the Chief Financial Officer. These took place following both the preliminary and half year results announcements in 2016. The Group engages Makinson Cowell, part of the KPMG Group, to advise and assist with communications with shareholders.

The Company's private registered shareholders hold, in aggregate, approximately 0.67% of the issued share capital. The Board is as interested in their views as it is in the views of institutional and corporate shareholders. All shareholders are free to put questions to the Board at the AGM. Questions asked in person at the AGM will receive a verbal response whenever possible. Otherwise, a written response will be provided as soon as practicable after the AGM. Questions asked at other times will normally receive a written response. Shareholders attending the AGM will have an opportunity to meet informally with the directors immediately after the meeting.

All information reported to the market via a regulatory information service also appears as soon as practicable on the Group's website at www.drax.com.

The directors consider that this Annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy. Pages 1 to 61 provide an assessment of the Group's affairs.

The Annual report and accounts is available to shareholders at least 20 working days before the AGM. Registered shareholders receive a Form of Proxy which allows them to vote for or against, or to abstain on each resolution. Particulars of aggregate proxies lodged are announced to the London Stock Exchange and appear on the Group's website as soon as practicable after the conclusion of the AGM.

BOARD OF DIRECTORS

CHAIRMAN

PHILIP COX CBE
Chairman

Responsibilities and skills:

Philip has significant board experience in both executive and non-executive capacities, and extensive experience in the power sector.

Appointment to the Board:

January 2015.

Appointment as Chairman:

April 2015.

Committee membership:

Nominations (Chair) and Remuneration Committees.

Current external appointments:

GPG, a joint venture between the Kuwait Investment Authority and Gas Natural Fenosa – a power generation company focused on emerging markets (Non-executive Chairman).

Previous roles:

Executive
International Power plc (Chief Executive Officer).
Ivensys plc (Senior Vice President, Operational Planning).
Siebe PLC (Finance Director).

Non-executive
Meggitt PLC (Non-executive director).
PPL Corporation, a US-listed energy utility company (Non-executive director).
Wm Morrison Supermarkets PLC (Non-executive director, Senior Independent Director and Chairman of the Audit Committee).
Wincanton plc (Non-executive director and Chairman of the Audit Committee).
Talen, a US-listed power generation company (Non-executive director and Chair of the Audit Committee).

Qualifications:

MA in Geography.
Fellow of the Institute of Chartered Accountants in England and Wales (FCA).

NON-EXECUTIVE DIRECTORS

TIM COBBOLD
Independent non-executive director

Responsibilities and skills:

Tim's blend of financial and engineering experience means that he is well placed to contribute significantly to the Board and its committees. His role as a serving Chief Executive in a different sector provides an added dimension to his contribution.

Appointment to the Board:

September 2010.

Committee membership:

Audit, Nominations and Remuneration Committees.

Current external appointments:

UBM plc (Chief Executive).

Previous roles:

Executive
De La Rue plc (Chief Executive).
Chloride Group plc (Chief Executive and following Emerson Electric's takeover of Chloride, Tim held a senior position in Emerson, responsible for the Chloride Group of companies).
Smiths Group plc, a number of senior financial and operational management positions over an 18 year period.

Non-executive
None.

Qualifications:

BSc (Hons) in Mechanical Engineering.
Fellow of the Institute of Chartered Accountants in England and Wales (FCA).

DAVID LINDSELL
Senior Independent non-executive director

Responsibilities and skills:
David's recent and relevant experience in the areas of finance and audit are a significant asset to the Board in his role as Chairman of the Audit Committee.

Appointment to the Board:
December 2008.

Committee membership:
Audit (Chair), Nominations and Remuneration Committees.

Current external appointments:
Premier Oil plc (Non-executive director and Chairman of the Audit and Risk Committee).
Cancer Research UK (Trustee and Chairman of the Audit Committee).
University of the Arts, London (Deputy Chair of Governors).

Previous roles:
Executive
Ernst & Young LLP (Partner).

Non-executive
Financial Reporting Review Panel (Deputy Chairman).
HellermannTyton Group PLC (Non-executive director).

Qualifications:
MA in History
Fellow of the Institute of Chartered Accountants in England and Wales (FCA).

TONY THORNE
Independent non-executive director

Responsibilities and skills:
Tony's experience of operating in different geographical territories is of great value to the Board as the Group's operations develop.

Appointment to the Board:
June 2010.

Committee membership:
Audit, Nominations and Remuneration (Chair) Committees.

Current external appointments:
South East Coast Ambulance Service (Chairman).

Previous roles:
Executive
DS Smith plc (Chief Executive and an executive director).
SCA Packaging Limited (President).
Shell International (Worked throughout the world in senior management roles, including strategic planning and President of the Shell companies in Mexico).

Non-executive
None.

Qualifications:
BSc (Hons) in Agricultural Economics.

EXECUTIVE DIRECTORS

DOROTHY THOMPSON CBE
Chief Executive, Drax Group

Responsibilities and skills:
Dorothy is responsible for all aspects of running the Group's business, including developing an appropriate business strategy for Board approval and securing its timely and effective implementation. She leads the executive team and takes responsibility for important external relationships with customers, suppliers, regulatory agencies and Government bodies.

Appointment to the Board:
October 2005, having joined the Group in September 2005.

Committee membership:
Executive Committee (Chair).

Current external appointments:
Court of the Bank of England (Non-executive director).
Eaton Corporation plc (Non-executive director).

Previous roles:
Executive
InterGen NV (Head of the European business and responsible for the management and operation of four gas-fired power plants, totalling some 3,160MW of capacity across the UK and the Netherlands).
Powergen plc (Assistant Group Treasurer).

Non-executive
Johnson Matthey Plc

Qualifications:
BSc (Hons) and MSc in Economics.

WILL GARDINER
Chief Financial Officer

Responsibilities and skills:
Will is responsible for the financial management of the Group, and for relationships with the Group's bankers and financial advisers. He has responsibility for the Financial Control and Planning, Corporate Finance and Investor Relations, Strategy and New Business, Group IT and Group Risk and Internal Audit functions.

Appointment to the Board:
November 2015.

Committee membership:
Executive Committee.

Current external appointments:
Qardio plc (Non-executive director).

Previous roles:
Executive
CSR plc (Chief Financial Officer)
BSkyB (Divisional Finance Director)
Easynet Group plc (Chief Financial Officer)
JP Morgan (Senior roles in the investment banking division, specialising in the telecoms and technology sections).

Non-executive
None.

Qualifications:
BA Harvard College in Russian and Soviet Studies.
MA John Hopkins School of Advanced International Studies in International Relations.

ANDY KOSS
Chief Executive, Drax Power

Responsibilities and skills:
Andy is responsible for the operation of the power plant and equipment. This includes all aspects of safety management, plant integrity, plant operations, engineering support, maintenance and plant design. He leads the power generation business unit which maximises shareholder value by driving efficiency and profitability.

Appointment to the Board:
January 2016, having joined the Group in June 2005.

Committee membership:
Executive Committee and Drax Power Management Board (Chair).

Current external appointments:
None.

Previous roles:
Executive
Drax Group (Director of Strategy, Head of Investor Relations, Group Treasurer and Head of Risk)
Provident Financial plc (Deputy Group Treasurer)
UBS, Dresdner Kleinwort Benson, Lehman Brothers (Various investment banking roles)
Coopers & Lybrand (Chartered Accountant).

Non-executive
None.

Qualifications:
BSc (Hons) in Maths, Operational Research, Statistics and Economics.
Associate of the Institute of Chartered Accountants in England and Wales (ACA).
Member of the Association of Corporate Treasurers (MCT).

EXECUTIVE COMMITTEE MEMBERS

MATTHEW RIVERS
Director of Corporate Affairs

Responsibilities and skills:

Matthew is responsible for the Group's sustainability policy, strategy and delivery of our essential assurance in this area, as well as for the Communications, Public Affairs and Regulation and Markets teams.

Appointment to the Executive Committee:

October 2013, having joined the Group in November 2011.

Committee membership:

Executive Committee and Billington Bioenergy (Chair).

Current external appointments:

None.

Previous roles:

Executive
UPM (Finland) (Director – Overseas Wood and Biomass Sourcing, Director – Energy Biomass).
UPM Tilhill (UK) (Managing Director – for the UK's largest private sector forest management and timber harvesting business).
Forestal Oriental (Uruguay) (Managing Director – responsible for plantation management and wood supply).

Non-executive
None.

Qualifications:

BSc (For) Hons, Forestry Aberdeen.
MBA, Strathclyde.
Fellow Institute of Chartered Foresters.
Chartered Environmentalist.

PETE MADDEN
Chief Executive, Drax Biomass

Responsibilities and skills:

Pete guides the business strategy and oversees day-to-day operations at two pellet plants and a port facility in the South Eastern United States, ensuring that they are environmentally sound, safe and professionally managed.

Appointment to the Executive Committee:

January 2016, having joined the Group in March 2015.

Committee membership:

Executive Committee and Drax Biomass Inc.

Current external appointments:

University of Georgia Center for Forest Business (Member, Advisory Board).
US Industrial Pellet Association (USIPA) (Member of the Board).
Forest History Society (Member of the Board)

Previous roles:

Executive
Plum Creek (USA) A number of roles including: Vice President, Renewable Energy and Supply Chain; Vice President, Operations Support; and Director, Regional Marketing, Operations, Resource Management, Materials Management and Corporation Planning.

Non-executive
None.

Qualifications:

BA Marlboro College.
MS (Forestry) University of New Hampshire.
MBA University of New Hampshire.

JONATHAN KINI
Chief Executive, Drax Retail

Responsibilities and skills:

Jonathan oversees business operations and champions Drax's retail strategy across Haven and Opus. He is responsible for pursuing increased business growth through small to medium-sized enterprise (SME) sectors, and for sustaining and growing Drax Retail's industrial and commercial (I&C) customer base.

Appointment to the Executive Committee:

September 2016, having joined the Group in January 2016.

Committee membership:

Executive Committee, Haven and Opus management boards (Chair)

Current external appointments:

None.

Previous roles:

Executive
Vodafone (Director of SME)
Virgin Media (Various commercial roles)

Non-executive
None.

Qualifications:

Bsc (Hons) in Mathematics, University of Manchester.
MBA, Henley Management College.
ACMA (CIMA qualified)

THE EXECUTIVE COMMITTEE

The Executive Committee

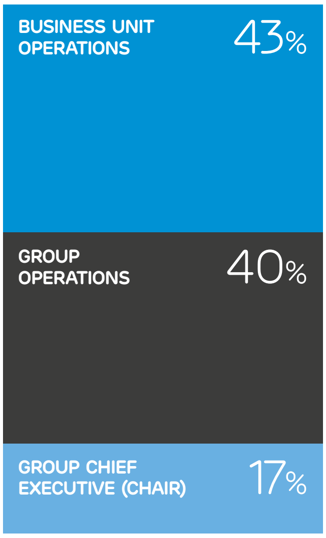
Each Drax business unit runs under its own management team and the shared services needed to support them are provided centrally through the Group Corporate function.

The Executive Committee focuses on the Group's strategy, financial structure, planning and performance, succession planning, organisational development and Group-wide policies.

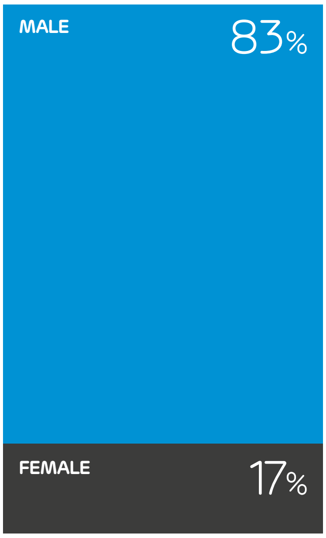
Composition

With the exception of Jonathan Kini, Chief Executive, Drax Retail (who was appointed a member in September 2016) all of those listed below served on the Executive Committee throughout the year and all continued to be members at the date of this report. Biographical details of Executive Committee members appear on page 70 (executive directors) and page 71 (senior management). Peter Bennell, who was Chief Executive, Haven Power and a member of the Executive Committee, retired in September 2016.

COMPOSITION



DIVERSITY



Executive Committee composition at 31 December 2016

Executive Committee members

Will Gardiner
Jonathan Kini
Andy Koss
Pete Madden
Matthew Rivers
Dorothy Thompson CBE

The Group Company Secretary acts as Secretary to the Executive Committee.

Executive Committee diversity at 31 December 2016

Executive Committee diversity

There are five male members and one female member of the Executive Committee.

Number of meetings

The Executive Committee has 12 scheduled meetings each calendar year and arranges additional meetings if needed.

Executive Committee attendance 2016

The table below shows the number of meetings and attendance at them by members of the Executive Committee during 2016.

	Date appointed as a member of the current Executive Committee	Maximum possible meetings(1)	Number of meetings attended	% of meetings attended
Dorothy Thompson CBE	1 March 2015	11	11	100%
Will Gardiner	16 November 2015	11	11	100%
Jonathan Kini	1 September 2016	4	4	100%
Andy Koss	1 March 2015	11	11	100%
Pete Madden	1 January 2016	11	11	100%
Matthew Rivers	1 March 2015	11	11	100%
Peter Bennell	1 March 2015	7	7	100%

Note:
(1) The maximum number of meetings that each individual was entitled to and had the opportunity to attend.

ROLES AND RESPONSIBILITIES OF THE EXECUTIVE COMMITTEE

DOROTHY THOMPSON

- **WILL GARDINER** Chief Financial Officer — Corporate including Finance, Risk, IT and Strategy
- **PETE MADDEN** President and Chief Executive, Drax Biomass — Drax Biomass
- **ANDY KOSS** Chief Executive, Drax Power — Drax Power
- **JONATHAN KINI** Chief Executive, Drax Retail — Haven Power Opus Energy Group
- **MATTHEW RIVERS** Director of Corporate Affairs — Corporate including Sustainability and Communications. Chairman of Billington Bioenergy

How the Executive Committee functions

The Executive Committee receives regular reports on performance against the Business Plan and periodic business reports from each of the business units. Papers are distributed in advance of meetings, to brief members on matters to be discussed. Members also receive presentations on various business issues by senior managers within the business units.

NOMINATIONS COMMITTEE REPORT

The Nominations Committee is crucial to ensuring that the Board has the right blend of expertise and experience and that it is ready to face the challenges of the future.

ROLE OF THE COMMITTEE

The Committee's principal responsibilities are to:

- keep under review the Board's structure, size and composition (including requisite skills, knowledge and experience it requires);
- ensure a rigorous succession planning process is in place for the directors and other senior managers, including the identification of candidates from both within and outside the Group.

Chairman
Philip Cox CBE

Committee members
Tim Cobbold, David Lindsell, Tony Thorne

Attending by invitation
Group Chief Executive, Head of Corporate HR

Number of meetings held in 2016
3

Terms of reference
The Committee's terms of reference are reviewed annually by the Committee and then by the Board. The terms of reference are available on the Group's website at www.drax.com.

The Group Company Secretary acts as Secretary to the Committee.

Attendance in 2016

	Date appointed a member	Maximum possible meetings	Number of meetings attended	% of meetings attended
Tim Cobbold	27 September 2010	3	3	100%
Philip Cox	22 April 2015	3	3	100%
Melanie Gee[1]	1 January 2013	2	2	100%
David Lindsell	1 December 2008	3	3	100%
Tony Thorne	29 June 2010	3	3	100%

Note:
(1) Melanie Gee retired as a director and Committee member on 20 April 2016.

The Chairman of the Committee reports on the Committee's proceedings to the following Board meeting.

The Committee has an annual programme of work which is designed to fulfil its principal duties. This programme reviews:

- **Re-election and appointment of directors** – The Committee met on 14 February 2017, following the completion of the 2016 Board evaluation and performance review process, (described at the end of this report) and determined that all of the directors who are the subject of annual re-election will retire at the forthcoming AGM and, being eligible, offer themselves for re-election. The Board evaluation and performance review concluded that the directors offering themselves for re-election continue to demonstrate commitment to their particular role and to perform effectively.

- **Size, structure and composition of the Board** – At its meeting in February 2016, the Committee concluded that the Board, constituted with three executive directors, four independent non-executive directors and a chairman who was independent on appointment, was appropriate for the Company at the time. The Board further considered the composition of the Board at its meeting in April 2016 following Melanie Gee's retirement from the

Board at the close of the AGM. Search processes are in progress for two new non-executive directors with specific backgrounds in retail and sustainability. At the Executive Committee level, the Committee reviewed the position of Chief Executive Officer of Haven following Peter Bennell's intention to retire. The Committee put in place a specific appraisal process to assess the suitability of Jonathan Kini to succeed Peter and this ultimately led to the appointment of Jonathan Kini as Haven's CEO in September.

- **Membership of Board committees** – It is the Board's policy to invite all independent non-executive directors to join the Audit, Nominations and Remuneration committees. The Committee reviewed this policy, and also the composition of the Board committees in light of Melanie Gee's retirement following the AGM. It was noted that the committees remained compliant with the provisions of the Code and thus no changes to the committees were recommended.

- **Succession planning** – The Committee reviews the succession plan at least annually. The Group has a well-established and robust succession planning process, which covers all Executive Committee members and their direct reports, as well as other individuals within the Group who have been identified as having longer-term potential for senior roles. In the Committee's opinion, the plan is well prepared and appropriate for the size of the Group's business and management structure, and there is a range of good candidates for senior roles. Any potential gaps are the subject of both internal development plans and/or selected external recruitment.

- **Board diversity** – In addition to the regular programme of work and the externally facilitated evaluation mentioned below, the Committee also considered the question of Board diversity in its widest sense, and gender diversity in particular. The Company has actively engaged with initiatives promoted by the Department for Business, Energy and Industrial Strategy to improve gender diversity at Board level. The Committee recognises the strength that can be achieved through diversity in the Group's management. In particular, the Board's policy is to ensure that the proportion of women is one of the considerations for Board and senior management appointments. That policy is implemented as part of the recruitment and selection process. Further details of gender diversity in the Group are included in the Employees section of the Sustainability review on page 44.

Non-executive directors

It is the Board's policy that each non-executive director will be appointed for a term of three years which, subject to the Board being satisfied as to the director's performance and commitment, and a resolution to re-elect at the appropriate AGM, may be renewed by mutual agreement. The Board will not normally extend the aggregate period of service of any independent non-executive director beyond nine years, and any proposal made to extend a non-executive director's aggregate period of office beyond six years is subject to review.

In 2016, two of our non-executive directors, Tim Cobbold and Tony Thorne, were both appointed for a third term (in addition to David Lindsell who was appointed for a third term in 2014). The Board has made this decision mindful of the Code which states that:

"Non-executive directors should be appointed for specified terms subject to re-election and to statutory provisions relating to the removal of a director. Any term beyond six years for a non-executive director should be subject to particularly rigorous review, and should take into account the need for progressive refreshing of the Board".

The reason why the Board has taken the step to appoint the non-executive directors named above for a third term is because the Group is at a key stage between the formulation of a new corporate strategy and its delivery. The Board feels that their continued service is vital to ensure that the Group benefits from the right blend of expertise and continuity of experience in its senior leadership as it makes and delivers these strategic moves.

Renewal and re-election

The Articles provide that one-third of directors shall retire by rotation each year and are eligible for re-election by shareholders at the AGM. In accordance with the Code, the Company will continue to propose all directors for annual re-election. Accordingly, each of Tim Cobbold, Philip Cox, Will Gardiner, Andy Koss, David Lindsell, Dorothy Thompson and Tony Thorne will retire at the forthcoming AGM and, being eligible, offer themselves for re-election.

Following the evaluation and review of the Board described below, I concluded that the directors offering themselves for re-election continue to demonstrate commitment, management and industry expertise in their particular role and continue to perform effectively. The re-election of each director is recommended by the Board. Details of the service contracts for the executive directors and letters of appointment for the non-executive directors are set out in a table on page 103.

The executive directors' service contracts and non-executive directors' letters of appointment are available for inspection by prior arrangement during normal business hours at the Company's registered office. They will also be available for inspection at the venue of the AGM, prior to the meeting, details of which are contained in the Notice of Meeting.

Board evaluation and performance reviews

The continued effectiveness of the Board is vital to the success of the Group. Drax is committed to continually improving the effectiveness of the Board and its Committees. This Committee took forward two key initiatives to further improve that effectiveness in 2016.

The first of these followed on from the internal Board evaluation initiated by the Committee during 2015. In 2016 we conducted an externally facilitated valuation of the Board.

Boardroom Review Limited was chosen to facilitate and conduct the evaluation. Boardroom Review Limited does not provide any other services to the Board. The recommended format was a facilitated workshop where all the directors and the company secretary took part. Ahead of this, each of the directors and the company secretary completed a detailed questionnaire providing information about how they viewed the role of the Board and how it functions.

The workshop took place in November and helped identify current strengths, future challenges, and provided valuable insights to enhance the Board's overall effectiveness. It was preceded and informed by conversations between Dr Tracy Long of Boardroom Review Limited and individual directors.

Following the workshop session, the Board reviewed the strengths of and challenges for the Board as well as the key themes that arose during the discussions. Recommendations for the future included selective invitations to advisers and outside experts to periodically present to the Board on key business and governance issues, and allowing more time on Board agendas for non-executive directors to discuss key issues without executive management present.

The Committee also initiated a review of the effectiveness of the Board, its committees and individual directors during 2016. The review concluded that all directors have a positive view of the effectiveness of the Board and its committees and that all directors continue to perform effectively and to demonstrate commitment to their roles. There is clear alignment of the directors' views of the Group's priorities and agreement that the key decisions of the Board focus on those priorities. Steps have been identified to improve processes and operation of meetings to facilitate greater focus on priorities and strategic matters. Measures have also been identified that will improve the quality of information provided to the Board to enhance its consideration of risk impacts and mitigation measures.

During the year, the Chairman held a meeting with the non-executive directors in the absence of the executive directors, and the Senior Independent Director held a meeting with the non-executive directors without the Chairman being present, as required by provision A.4.2 of the Code.

Directors' development

The Board is committed to the development of all employees and directors and has reviewed, and will periodically continue to review, each director's development requirements and make appropriate arrangements to address them. All new directors receive a full induction programme including wider background briefings on the Group's activities, meetings with key managers and visits to the Group's sites.

In addition, each non-executive director visits operational sites both in the UK and the US. In 2016 the Board visited operational and administrative sites in the US, and over a three-day period carried out visits to Drax Biomass's operations and reviewed the wider sustainability programme and activities. Periodically, the non-executive directors also meet with senior management to be briefed on the Group's business and specific Board training days are arranged covering key relevant topics.

This report was reviewed and approved by the Nominations Committee on 15 February 2017.

Philip Cox CBE
Chairman of the Nominations Committee

AUDIT COMMITTEE REPORT

Sound risk management and internal control systems are essential to enable the Group to achieve its objectives, while proper accountability to shareholders requires fair and balanced performance reporting.

ROLE OF THE COMMITTEE

The Committee assists the Board to fulfil its oversight responsibilities. Its primary functions are to:

– monitor the integrity of the financial statements and other information provided to shareholders;
– review significant financial reporting issues and judgements contained in the financial statements;
– advise the Board on whether the Committee believes the annual report and accounts are fair, balanced and understandable;
– maintain an appropriate relationship with the Group's external auditor and review the effectiveness and objectivity of the external audit process;
– review the systems of internal control and risk management; and
– monitor and review the effectiveness of the internal audit function, review the internal audit plan and all internal audit reports and review and monitor management's responses to the findings and recommendations of the internal audit function.

Terms of reference

The Committee's terms of reference are reviewed annually by the Committee and then by the Board. The terms of reference are available on the Group's website at www.drax.com.

Chairman

David Lindsell

Committee members

Tim Cobbold and Tony Thorne, both of whom are independent non-executive directors.

The Board is satisfied that the Committee's membership has the recent and relevant financial experience required by the Code.

Attending by invitation

Chairman of the Board, Group Chief Executive, Chief Financial Officer, Group Financial Controller, Group Finance Manager, Head of Group Risk and Internal Audit, External auditor (Deloitte).

Number of meetings held in 2016

4

The Group Company Secretary acts as Secretary to the Committee.

Attendance in 2016

	Date appointed a member	Maximum possible meetings	Number of meetings attended	% of meetings attended
Tim Cobbold	27 September 2010	4	4	100%
Melanie Gee[1]	1 January 2013	2	2	100%
David Lindsell	1 December 2008	4	4	100%
Tony Thorne	29 June 2010	4	4	100%

Note
(1) Melanie Gee retired as a director and Committee member on 20 April 2016.

The Chairman of the Committee reports the Committee's deliberations to the following Board meeting. The minutes of each Committee meeting are circulated to all members of the Board.

In undertaking its duties, the Committee has access to the services of the Chief Financial Officer and the Group Company Secretary and their resources, as well as access to external professional advice.

Main activities during the year

During the year, the Committee undertook its duties in accordance with an annual work plan, which is agreed in November for the following calendar year and reviewed at each meeting. The main areas of work undertaken by the Committee at each of its meetings during 2016 are set out in the table below.

Meeting	February	April	July	November
Item under review	– Year-end review of accounting issues and judgements (2015) – Consideration of the 2015 annual report, financial statements and preliminary results announcement – Review of the effectiveness of internal controls and consideration of fraud – Review of 2016 internal audit strategy and risk mapping – Review of final report from Deloitte on their audit findings – Assessment of the effectiveness of the external audit process – Review of the Audit Committee's effectiveness	– Review of Senior Accounting Officer reporting – Review of management update on year-end accounting issues and judgements and of the potential impact of new accounting standards – Review of the auditor independence policy – Review of the whistleblowing reporting policy – Review of an activity report from the Ethics and Business Conduct Steering Committee – Received an update regarding the tender process for the external audit engagement – Approved the Internal Audit Charter	– Review of accounting issues and judgements affecting the 2016 interim financial statements – Consideration of the half-yearly financial report – Review of a report from Deloitte on their interim review findings – Review of a report covering biomass sustainability assurance – Review of the Audit Committee's terms of reference – Review of the Group's proposed accounting policy for the CfD – Received a business update presentation from Haven, covering key risks and controls – Review of audit tender conclusions and recommendation to the Board	– Review of accounting issues and judgements affecting the 2016 financial statements – Review of Deloitte planning report on the 2016 audit, their terms of engagement and proposed audit fees – Review of the composition and qualifications of the Group's finance teams – Received a business update from Drax Power, covering key financial risks and controls – Review of the internal audit plan for 2017–18 – Review and approval of the external auditor's terms of engagement – Review of the effectiveness of the Group's internal controls and risk management systems and the effectiveness of its procedures for detecting fraud and preventing bribery – Review of the response to a letter from the Financial Reporting Council (FRC) regarding the Group's 2015 Annual report

In addition, there are a number of routine items which are put to each meeting as follows:

– a review of the minutes and actions from previous meetings;
– reports from the internal audit function on its progress with the programme for the year, including fee analysis and new internal audit reports; and
– the Committee's rolling annual plan review.

Between the year-end date and the date of the approval of the annual report and accounts, the Committee met in January 2017 to review the contents of the shareholder circular in relation to the Opus acquisition and recommend the Board approve the circular, and in February 2017 principally to review the draft 2016 Annual report and accounts and the external auditor's findings.

The Committee continues to focus on strategic risk areas, such as biomass sustainability reporting, as well as ensuring the provision of a core compliance assurance service. No significant weaknesses were identified in any of the internal audit reports, although improvements in processes and procedures were made as a result of reviews. At its meeting in July 2016 the Committee received and reviewed an independent report concerning biomass sustainability controls. The report raised no material weaknesses in policy or approach but did highlight the key areas of judgement and risk within the process. Similar to routine internal audit reviews, certain improvements in processes and procedures were implemented as a result of the report's recommendations. During 2016, the Committee also received updates on financial risks and controls from each of the Group's primary business units. Drax Power and Haven Power attended Committee meetings and Drax Biomass presented to the Committee as part of a Board visit to the US in October.

In July 2016, the Committee reviewed and approved management's proposed accounting policy for the CfD contract, which is described on page 127. The Group's principal accounting policies and the judgements and assumptions made in the process of applying them are set out in the notes to the accounts. In respect of all such matters, including the accounting treatment of the CfD, the external auditor concurred with the judgements made by management and the Committee was satisfied that the accounting policies were applied appropriately, and that the accounting estimates and judgements made were appropriate. In addition, the Committee satisfied itself as to the independence and objectivity of the external auditor on the basis set out below under "Independence of the external audit".

In October 2016, the Group received a letter from the FRC's Corporate Reporting Review team, requesting information about certain matters arising from their review of the 2015 Annual report and accounts. As a result of correspondence and discussions with the Review team some additional information, relating in particular to the effectiveness of power generation using biomass in reducing carbon emissions and to asset impairment testing, has been included in the 2016 Annual report and accounts. The Committee reviewed and approved the Group's responses to the FRC's enquiries.

The Committee has a forward programme of specific review areas, with a focus on risk management processes, internal control systems, and financial reporting aspects. In addition, the Committee monitors the Group's general internal control environment on an annual basis, including risk management structures, policies and processes, the overall financial control framework, key operational controls including production integrity, IT and environmental controls, and procedures in relation to bribery, fraud and any non-compliance.

During 2016, the Committee reviewed the Group's preliminary results announcement, annual report and accounts, and half-year results announcement. At these meetings, the Committee received reports from management and the external auditor on the application of accounting policies on significant estimates and judgements made in preparing the financial statements, and on the methods used to account for any significant or unusual transactions.

Reviewing the 2016 annual report and accounts

At its meeting in February 2017, the Committee reviewed the content of the 2016 Annual report and accounts, alongside a paper on accounting issues and judgements affecting the accounts and a report from Deloitte LLP setting out their audit findings. The significant issues and judgements considered were as follows:

Matter	Issue and nature of judgement	Factors considered and conclusions reached
Carrying value and useful lives of fixed assets	In 2015 the market capitalisation of the Group fell materially below the carrying value of the Group's net assets. Whilst the shortfall has reduced considerably during 2016, this remains the case at the balance sheet date. In addition, commodity markets are weak and the substantial weakening of Sterling against both the Euro and US dollar in the second half of 2016 indicated a potentially material increase in the long-term costs of fuel for our generation business, which are predominantly priced in these currencies. As a result, in accordance with the requirements of IFRS, management conducted an impairment review in respect of the Drax Power cash-generating unit (CGU). They did so by comparing the present value of future cash flows the CGU with the carrying value of its tangible and intangible assets. The assumptions that underpin such calculations are, by their nature, dependent upon application of judgement and are thus subject to uncertainty. In particular this is because observable market information is only available for a limited proportion of the remaining lives of the Group's power generation assets.	Management presented an overview of the methodology and most critical assumptions to the Committee meeting in November 2016. The Committee reviewed an updated report at its meeting in February 2017 that considered refinements in assumptions and key judgements up to the present time, as described in note 2.4. It was noted that the cash flows that underpin the value in use calculation for the Drax Power CGU were derived from the Group's five-year business plan, which was subject to review by the Board in January 2017. This review included challenge of the key assumptions, including commodity and currency forward curves, the expected useful life of the coal generating units (see note 3.1) and post-2027 revenue sources. After challenging management, regarding these longer-term assumptions, the Committee concluded that a reasonable, supportable and consistent approach had been taken in preparing the review and that there was no current indication of impairment.
Derivative financial instruments	The Group makes extensive use of derivative financial instruments in order to manage key risks facing the business and its balance sheet includes significant assets and liabilities arising from derivatives which are stated at their fair value. In particular, the asset values of forward foreign currency purchase contracts increased substantially in the period following the weakening of Sterling. Changes in the fair value of such instruments are recognised in the income statement or when the specific criteria for hedge accounting are met, in the hedge reserve. The fair values for derivative financial instruments are determined using forward price curves and, where an instrument incorporates an element of optionality, an option pricing model. The inputs to these calculations include assumptions regarding future transactions and market movements, as well as credit risk, and are therefore subjective.	The Committee reviewed the Group's derivative position in February, July and November 2016 having regard in particular to the critical judgemental areas described in note 7.2 and considered the position as at 31 December 2016 at its meeting in February 2017. At each meeting, management explained the trends in market prices that underpinned changes in the fair value of the derivative portfolio and highlighted any new types of derivative instrument for the Committee's consideration. The Committee concluded that the fair value calculations had been performed in a reasonable and consistent manner based on quoted market prices as explained in note 7.2 and that the system of controls in place was fit for purpose. Accordingly, it was concluded that the amounts included in the financial statements were appropriate.

Matter	Issue and nature of judgement	Factors considered and conclusions reached
Valuation of ROC assets	The Group receives ROCs for generating electricity from sustainable biomass. The Group's balance sheet contains a material amount of such assets at the end of December 2016. ROC assets are initially valued at fair value and subsequently written down to net realisable value where appropriate. These calculations require an element of judgement in considering probable future sales prices in the market.	The Committee reviewed papers presented by management at its meetings in February, July and November, which set out the current balance sheet valuation and the key underlying assumptions that drive the carrying value, including the assessment of likely future sales prices of ROCs. At its meeting in February 2017, the Committee reviewed the specific assumptions that directly impact the amounts recognised in the 2016 financial statements, as explained in note 3.2. The Committee concluded that the judgements made in valuing ROC assets were reasonable, supportable and consistent and that, accordingly, the values included in the financial statements were appropriate.
Existence and valuation of fuel inventories	The Group carries a material amount of fuel inventories (predominantly coal and biomass in the form of compressed wood pellets) which are measured at the lower of their weighted average cost and net realisable value. Whilst value is largely based on observable costs, the nature and characteristics of the inventories mean that determining the volume of inventory at any given time is subject to a degree of estimation. Accordingly, while both coal and biomass stocks are measured using equipment regularly calibrated to industry standard levels of tolerance, as explained in note 3.3 the potential for actual results to vary from initial calculations remains. Stocks are surveyed at the balance sheet date by either an independent third party or electronic scanning equipment and provisions made where appropriate. However, both methods rely on assumptions regarding density of the fuel surveyed.	The Committee reviewed the processes, including judgements, estimates and assumptions made, in respect of fuel inventory valuation at its meetings in February, July and November in 2016. At its meeting in February 2017, the Committee reviewed the position and specific judgements made in respect of the 2016 financial statements. Having challenged management on the appropriateness of the measurements used in determining inventory volumes, the Committee concluded that the process and approach followed by management had been performed in a reasonable and prudent manner.

Explanations of the critical accounting judgements, estimates and assumptions are set out in detail throughout the notes to the consolidated financial statements, with a summary on pages 117 and 118.

The Committee also reviewed the underlying process, internal controls, forecasts and relevant assumptions made in preparing the Viability Statement, disclosed on page 54 of this Annual report. Having challenged the assumptions made in this process and considered the appropriateness of the three-year period of assessment, the Committee concluded that the process supporting the Viability Statement was robust.

In addition, other matters relating to the application of accounting policies or accounting treatment were considered during the year at the February, July and November 2016 meetings, and again at the February 2017 meeting in relation to our financial statements. These included:

- the accounting judgements, estimates and assumptions in relation to revenue recognition, retirement benefit obligations and taxation. Further information on these areas can be found in the consolidated financial statements; and
- other accounting issues, relating to application of accounting policies or accounting treatment. Where applicable, our accounting policies are set out in the relevant note to the consolidated financial statements.

The Committee met twice in the absence of management with each of the external auditor (February and July) and Head of Group Risk and Internal Audit (April and November). No matters of concern were drawn to the Committee's attention at any of these meetings. The Committee's understanding with both the external and internal auditor is that, if they should at any time become aware of any matters giving them material concern, they will immediately draw it to the Committee's attention via the Chairman of the Committee. Nothing was reported in this way during the year.

Review of Audit Committee effectiveness by members

In line with the FRC's Guidance on Audit Committees, the Committee reviewed its own effectiveness and concluded that the composition of its membership, the manner in which it operates and the reviews that it undertakes throughout the year all contribute to the continued effective functioning of the Committee.

Fair, balanced and understandable view

The Committee reviewed the content of this annual report and accounts and advised the Board that, in its view, taken as a whole, it is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

External auditor effectiveness

The Committee reviewed the effectiveness of the external auditor, Deloitte LLP, who have performed the role continuously since the Company's listing in 2005. This process incorporated feedback from management and key individuals across the Group, as well as the Committee's own experience. The assessment considered the independence and objectivity of Deloitte, the robustness of the audit process, the quality of delivery of the audit plan, the quality of reporting on findings and recommendations to the Committee and management, and the experience and expertise of the audit team and the quality of service provided.

Independence of the external audit

The Group has an Auditor Independence Policy (the Policy), in accordance with which the Committee annually reviews the quality and cost-effectiveness of the external audit and the independence and objectivity of the external auditor. The Policy can be found on the Company's website at www.drax.com.

The provisions of the Policy include:

- seeking confirmation that the auditor is, in its professional judgement, independent of the Group, and obtaining from it an account of all relationships which may affect the firm's independence and the objectivity of the audit partner and staff;
- a policy governing the engagement of the auditor to conduct non-audit work, under which:
  - the auditor may not be engaged to provide certain categories of work, including those where they may be required to audit their own work or make management decisions, or where the auditor would act in an advocacy role for the Group;
  - there is a clear approval process for engaging the auditor to conduct other categories of non-audit work, subject to financial limits;
  - all engagements of the auditor to conduct non-audit work are reported to the next meeting of the Committee; and
  - the balance between the fees paid to the external auditor for audit and non-audit work is monitored by the Committee.

The Committee receives reports from the external auditor on its own processes and procedures, to ensure its independence and objectivity and to ensure compliance with the relevant standards.

Details of the amounts paid to the external auditor during the year for audit and other services are set out in note 2.2 to the consolidated financial statements on page 127.

No contractual obligations exist that restrict the Group's choice of external auditor.

Audit tendering and rotation

The Group has complied with the provisions of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014.

In accordance with the requirements of Regulation 537/2014 of the European Parliament and Council, we conducted a tender process for the external audit of the 2017 financial statements during the year. This process was led by the Chair of the Audit Committee and involved a tender committee comprised of management from across the Group's finance and risk functions.

At its meeting in July 2016 the Committee reviewed an update on the tender process. In November 2016 the Chair presented a report outlining the tender committee's findings and recommendations. The Audit Committee debated these findings, before agreeing to recommend to the Board that Deloitte LLP should be reappointed as external auditor for the 2017 financial statements.

The recommendation will be put to shareholders at the AGM in April 2017.

Internal audit

From 2016, the Group's internal audit function moved to a co-sourced model led by the Head of Group Risk and Internal Audit, having previously been undertaken by Grant Thornton UK LLP.

As part of the transition, the Committee reviewed and approved the Group's Internal Audit Charter strategy and initial plan for areas of review in 2016 and 2017.

Under the new model, the internal team conducts core financial control reviews. Reviews of specialist technical areas are outsourced to firms with appropriate experience and qualifications.

The Committee receive reports at each meeting regarding the internal audit programme and reviews undertaken. Recommendations are made to management for control improvements as appropriate. Topics dealt with by internal audit reports reviewed by the Committee during 2016 included:

- retail pricing model and advanced metering roll-out;
- ROC process controls self-assessment;
- physical fuel trade settlement;
- key financial controls over expenditure and payroll in the Retail business; and
- generation stores and non-spares stock.

In addition, at the April and November meetings the Committee received reports detailing progress with implementing recommendations previously raised by internal audit. Following the most recent of these updates, in November 2016, the Committee was satisfied that management is taking appropriate steps to deal with the recommendations raised.

The Chairman of the Committee, independent of management, maintains regular and direct contact with both the internal and external auditor.

This report was reviewed and approved by the Audit Committee on 15 February 2017.

David Lindsell
Chairman of the Audit Committee

REMUNERATION COMMITTEE REPORT

The management team made significant advances on strategy and continued, along with the staff as a whole, to deliver a highly effective operational performance across all business areas in the Group.

ROLE OF THE COMMITTEE

The Committee's principal responsibilities are to:
- recommend to the Board the remuneration strategy and framework for the executive directors and members of the Executive Committee;
- determine, within that framework, the individual remuneration packages for the executive directors and members of the Executive Committee;
- approve the design of annual and long-term incentive arrangements for executive directors and members of the Executive Committee, including agreeing the annual targets and payments under such arrangements;
- determine and agree the general terms and conditions of service and the specific terms for any individual within the Committee's remit, either on recruitment or on termination;
- determine the policy for, and scope of, executive pension arrangements; and
- oversee any major changes in employee benefit structures throughout the Group and review remuneration trends across the Group.

Chairman
Tony Thorne

Committee members
Tim Cobbold, Philip Cox, David Lindsell

Attending by invitation
Group Chief Executive, Head of Corporate HR, external remuneration advisers

Number of meetings held in 2016
5

Terms of reference
The Committee's terms of reference are reviewed annually by the Committee and then by the Board. The terms of reference are available on the Group's website at www.drax.com

The Group Company Secretary acts as Secretary to the Committee.

Attendance in 2016

	Date appointed a member	Maximum possible meetings	Number of meetings attended	% of meetings attended
Tim Cobbold	27 September 2010	5	5	100%
Philip Cox	22 April 2015	5	5	100%
Melanie Gee[1]	1 January 2013	2	2	100%
David Lindsell	1 December 2008	5	5	100%
Tony Thorne	29 June 2010	5	5	100%

Note:
(1) Melanie Gee resigned as a director and Committee member on 20 April 2016.

This Directors' Remuneration Report has been prepared in accordance with Schedule 8 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, as amended (the Regulations) and the provisions of the Code.

Annual statement to shareholders

This report reviews the key matters considered by the Remuneration Committee in the past year and the future matters we expect to consider. During the year, the Committee, in addition to its normal responsibilities, conducted a thorough review of the Group's remuneration policy.

The management team performed strongly in 2016 and this is reflected in the year's pay outcomes. Commodity markets remained challenging and there was a delay in the approval of the important CfD, by the European Commission. The mitigating actions taken by management, combined with good implementation, meant that the Company had a strong performance and outcome, compared to plan. In addition to high operational performance, there was a good advance on the strategic front. The announced strategic moves, coupled with the improved outlook for earnings, gave a healthy boost to the share price.

Annual assessment of performance

Performance areas of particular note in the year included the excellent safety result. At Drax Power, income lost through delays to the state aid approval of the CfD was more than offset by securing high ancillary service revenues and good use of coal unit flexibility. The CfD was finally approved, in December 2016, at the contract strike price of £100/MWh. At Drax Biomass although availability was below target, quality was above target. Haven's results were pleasing with continued growth and at improved margins.

With Drax now "predominantly biomass fuelled", the strategy the Group launched in 2012 has completed. Management had been working with the Board for some time on a new strategy. This was launched publicly in December and is described earlier in the Annual report. The acquisitions of Opus and four OCGT projects, plus the advice that the Group was actively looking at securing further US pellet production, were all initiatives consistent with the new strategy and were well received by the market.

There is a detailed review of performance against our balanced scorecard measures on page 98. Components within the scorecard can be scored between 0 and 2.0. A score of 1 represents an on-target performance. For 2016 the Board assessed the overall performance at 1.3.

The score is applied both to the annual bonus and the Bonus Matching Plan (BMP). For the purposes of the annual bonus the overall score in any year is capped at 1.5. There is no cap on the annual score when applied to the BMP scorecard, but there is a cap of 1.5 on the average for the three years.

Based on performance, a corporate score of 1.3 out of 2 and personal score of 1.35 out of 1.5 was agreed by the Committee, resulting in annual bonuses of approximately 88% of maximum. The Committee believes that this bonus outcome fairly reflects what has been a strong performance, in terms of what management has achieved against the Business Plan and the strategy, the way in which they have led the employee base and the shareholder value created during the year.

Long-term assessment of performance

BMP awards made in 2014 were tested at the end of 2016 by reference to relative Total Shareholder Return (TSR) performance (50%) and on the three-year average of the corporate scorecard (50%). The Company's TSR over the period was below the median of the comparator group, and the Committee therefore confirmed that none of the TSR element of the award would vest. The average corporate scorecard outcome over the same period was 1.09 out of 1.5, and therefore 15.43% of the executive directors' 2014 BMP awards will vest.

The Committee viewed the formulaic vesting outcome as a reasonable reflection of performance over the three-year period, acknowledging that the share price has been affected by external events during the last three years, but that significant progress has been made against strategic and financial targets set out in the Business Plan.

No discretion was exercised in determining the remuneration payouts.

Base salaries

Base salaries were reviewed with effect from 1 April 2016. Dorothy Thompson, Will Gardiner and Andy Koss did not receive any salary increase, while the average increase for the wider workforce was 2.7%.

Review of remuneration policy

While the Committee has been pleased with shareholders' support over the life of the current policy, we need to ensure that our remuneration arrangements remain fit for the future and align with good practice. To maintain remuneration arrangements that robustly measure and reward business and shareholder outcomes, we fully reviewed the remuneration policy applying to directors in 2016.

In summary, the main changes proposed for 2017 onwards are as follows:

- decoupling the annual bonus and the BMP, with the introduction of a new Performance Share Plan (PSP) and Deferred Share Plan (DSP), along with a reduction in the maximum individual limit which can be granted from 225% to 175% of an executive's salary;
- adjusting the vesting schedules to give a better balance between performance and reward, while introducing a two-year holding period post the three-year vesting of PSP shares;
- increasing the executive shareholding guideline to 200% of salary; and
- changing the vesting arrangements for deferred bonus awards on cessation of employment, by removing any pro-rating for time, but retaining the normal vesting date, rather than paying out awards immediately on leaving.

The Committee believes that the proposals strengthen the alignment of executive remuneration with delivery of the business strategy and shareholder value. In particular, we have:

- simplified the arrangements by introducing a market-standard performance share plan;
- reduced maximum executive remuneration in line with investor sentiment;
- increased the alignment with long-term shareholder value; and
- moved into line with current corporate governance best practice.

Further details of the proposed changes are provided in the policy section of this report on page 86.

Summary

I, and the other members of the Committee, are satisfied that the 2016 remuneration outcomes fairly reflect corporate and personal performance. We are confident that our new policy provides the right incentive to management, aligns well with shareholder interests and brings us closely in line with best practice.

I was very pleased with the level of support received from investors during consultations over the new remuneration policy. We will continue to monitor changes in executive remuneration and listen to the regular feedback from shareholders, to ensure that our remuneration policy remains in line with good practice. Overall, we will continue to make sure that our executives' pay reflects performance achieved.

At a glance

The following is an overview of our remuneration framework applying from 2017 onwards, under the new directors' remuneration policy to be put to shareholders at the Company's AGM in April 2017.

Remuneration component and link to strategy	Key features
Base salary, benefits and pension Payable to attract, reward and retain the right calibre of executive to deliver the leadership and management needed to execute the Group's vision and Business Plan.	Market competitive elements to attract the right calibre of executives (including health cover, car and defined contribution retirement benefits).
Annual bonus The award of annual bonus is directly linked to personal performance and to achieving the annual Business Plan targets.	**Maximum annual bonus potential** is 150% of salary for the Group Chief Executive and 140% for other executive directors. **Performance conditions** include a corporate scorecard and personal score and payout is determined based on a multiplicative formula. **Deferral:** 65% of annual bonus earned is paid in cash and 35% is deferred in shares, which vest after three years subject to continued employment or "good leaver" termination provisions.
Performance Share Plan (replaces Bonus Matching Plan) The PSP links long-term share-based incentives to TSR and the achievement of Business Plan strategic targets.	**Normal annual awards** are 175% of salary. **Vesting** occurs after three years, based on TSR relative to a FTSE 350 comparator group (50%) and the average corporate scorecard over the period (50%). Awards are subject to a two year holding period.
Shareholding guidelines The Group's share ownership guidelines align the interests of executives with shareholders.	Executives are expected to retain shares to the value of 200% of base salary.

Incentive outcomes for 2016

Annual bonus

Area	Weighting	Score/Outcome
Safety	5%	1.53
Finance	40%	1.61
Regulation	20%	0.90
General	5%	1.30
Business units	30%	1.17
Overall "corporate score" (CS) (maximum 2)		1.30
Executive director "personal score" (PS) (maximum 1.5)		1.35
Bonus outcome as % of maximum (=CS x PS x 50%)		**8.8**
Range of bonus outcomes as % of salary		**123–132%**

See page 98 for further details

BMP

Area	Weighting	Score/Outcome
2014 corporate score		1.22
2015 corporate score		0.76
2016 corporate score		1.30
Average corporate score (maximum 1.5)	**50%**	**1.09**
Relative TSR performance	**50%**	**0%**
BMP outcome as a % of maximum		**15.43%**

See page 91 for further details

Single total figure remuneration table for 2016

	Remuneration element (£000)						
Executive director (Role)	Base salary	Pension	Annual bonus[1]	BMP[2]	Other benefits	**2016 Total**	2015 Total
Dorothy Thompson (Chief Executive, Drax Group)	574	115	756	60	76	**1,581**	1,248
Will Gardiner (Chief Financial Officer)	390	78	479	–	24	**971**	96[3]
Andy Koss (Chief Executive, Drax Power)	310	62	381	16	21	**790**	n/a[4]

Notes:
(1) Bonus is the cash value of the annual bonus payable in respect of performance in the relevant year, including the value of bonus deferred and paid in shares after three years subject only to continued service.
(2) BMP is the value of the BMP Matching Awards vesting in March 2017, together with the dividend shares in relation to those vested shares. The value is calculated based on the average share price over the last quarter of 2016.
(3) Will Gardiner was appointed as a director on 16 November 2015.
(4) Andy Koss was appointed as a director on 1 January 2016.

Directors' remuneration policy

This remuneration policy, subject to shareholder approval at the 2017 AGM, will be effective from immediately after the AGM on 13 April 2017 and will be binding upon the Group until the close of the 2020 AGM. There are no planned changes to the policy over the three-year period to which it relates.

The core principles of the remuneration policy are set out below:

– making sure that executive remuneration is linked strongly to performance and the achievement of strategic objectives;
– ensuring transparency in executive pay reporting through simplification in design and appropriate reporting;
– securing and retaining top talent; and
– maintaining flexibility, to recognise the uncertain business environment, whilst ensuring that remuneration outcomes are aligned to shareholder interests.

Key components of remuneration

The remuneration policy for executive directors has been designed to support the delivery of strong business performance and the creation of shareholder value. We set out in the table below the policy relating to the key components of the remuneration policy for executive directors, and in the notes following the table we comment on differences between this policy and that for the remuneration of employees generally.

Base Salary

Base salary helps to attract, reward and retain the right calibre of executive to deliver the leadership and management needed to execute the Group's vision and Business Plan.

Practical operation

Base salary reflects the role, the executive's skills and experience, and market level. It is paid in 12 monthly instalments.

To determine the market level, the Committee reviews remuneration data on executive positions at companies which the Committee considers to be appropriate comparators.

The comparator companies are selected, with advice from the Committee's remuneration advisers, taking into account factors such as, but not limited to, sector, size, and international presence.

On appointment, an executive director's base salary is set at the market level, or below if the executive is not fully experienced at this level.

Where base salary on appointment is below market level to reflect experience, it will be increased over time to align with the market level, subject to performance.

Base salaries of all executive directors are generally reviewed once each year, with increases applying from April. Reviews cover individual performance, experience, development in the role and market comparisons.

Maximum potential value

The base salaries of executive directors in post at the start of the policy period, and who remain in the same role throughout the policy period, will not usually be increased by a higher percentage than the average annual percentage increase in salaries of all other Group employees in the Group.

Exceptions to this, subject to performance and development, are where:

(i) An executive director has been appointed at below market level to reflect experience. Under this scenario, increases will be capped at 5% above the average annual percentage increase in salaries of all other Group employees.

(ii) An executive director has been promoted internally and their salary is below market level. Under this scenario, increases will not be capped and the Committee can increase base salary to the market level within an appropriate timeframe.

Performance measures

No performance measures apply.

Annual bonus

The award of annual bonuses is directly linked to personal performance and to achieving the annual Business Plan targets.

The multiplicative formula is designed to ensure that bonus payments for high personal performance are moderated where business performance is below target, or vice versa.

The aim of the deferred portion of annual bonus is to further align executives to shareholders' interests, by linking share-based reward to long-term sustainable performance.

Practical operation

65% of annual bonus earned is paid in cash, normally three months after the end of the financial year to which it relates.

35% of annual bonus earned is deferred in nil cost awards over shares under the Deferred Share Plan (DSP), which vest after three years subject to continued employment or "good leaver" termination provisions.

The DSP is proposed to be introduced for 2017, as a vehicle for deferring the relevant proportion of annual bonus in shares.

Annual bonus earned (subject to the maximum opportunity) is:

Target bonus x corporate score x personal score.

Target bonus is 50% of maximum.

Corporate score ranges from zero to 2.0.

Each measure in the corporate scorecard is assigned a weighting and three performance levels (low, target and stretch). The score is zero if performance is below the low target, 1 if performance is at target and 2 for stretch performance. Although the individual elements are scored up to 2, the bonus is capped at 1.5

Personal score ranges from zero to 1.5.

The score is zero if performance is below threshold, 1 if performance is at target level and 1.5 for exceptional performance of the executive team or individual.

Dividends in respect of the deferred shares are reinvested in additional shares, which vest when the deferred shares vest.

In certain circumstances, the Committee can apply clawback to any annual bonus awards, as set out in the notes to the policy table.

Summary corporate scorecard and performance results are published in the Annual report on remuneration.

The Committee will review the formulaic outcome of the Annual bonus and can amend the final outcome to ensure that bonus payments reflect overall performance. The use of such discretion will be explained fully in the relevant Annual report on remuneration.

Maximum potential value

Role	Maximum bonus potential (% of base salary)
Chief Executive, Drax Group	150%
Other executive directors	140%

There is no payment for below threshold performance.

Performance measures

Corporate score is based on performance against the corporate scorecard of strategic and Business Plan targets set by the Committee each year, in conjunction with the Board. Performance measures include financial, production, strategic and other Business Plan objectives. Typically at least 30% of the corporate scorecard is based on financial objectives, around 30% on strategic goals and at least 30% is based on specific objectives within business units, but the Committee has discretion to vary the weightings from year to year.

The corporate scorecard is amended each year, in line with business strategy and objectives.

Personal score. The Committee determines the personal objectives for the Group Chief Executive, who in turn proposes personal objectives for the other executive directors, which are reviewed and approved by the Committee. Generally, all executive directors will be awarded a single score based on their collective performance in providing effective day-to-day leadership of the Group as a unified leadership team. Personal scores may differ in circumstances of exceptional over or under performance.

In exceptional circumstances such that the Committee believes the original measures and/or targets are no longer appropriate, the Committee has discretion to amend performance measures and targets during the year.

Drax 2017 Performance Share Plan (PSP)

The PSP is the Company's new long-term incentive plan. It replaces the legacy BMP and links long-term share-based incentives to TSR and to the achievement of Business Plan strategic targets.

Practical operation

The PSP is a new long-term performance share plan, which is being put to shareholders for approval at the 2017 AGM.

Under the PSP, executive directors receive an annual grant of nil cost conditional awards over shares.

Shares vest on the third anniversary of the grant, subject to continued service or "good leaver" termination provisions, and the achievement of performance conditions over a three-year period determined by the Committee. Vested awards are subject to a further holding period of two years.

Dividends or dividend equivalents (which may assume notional reinvestment) are paid on PSP awards.

The Committee will include an override provision in each grant under the PSP. This will give the Committee discretion to determine that no vesting shall occur, or that vesting shall be reduced, if there are circumstances (relating to the Company's overall performance or otherwise) which make vesting when calculated by reference to the performance conditions alone inappropriate.

In certain circumstances, the Committee can apply malus or clawback to unvested/vested awards, as set out in the notes to the policy table.

The Committee reserves discretion to:

(i) amend the performance conditions/targets attached to outstanding awards granted under this policy, in the event of a major corporate event or significant change in economic circumstances, or a change in accounting standards having a material impact on outcomes; and

(ii) adjust the vesting of PSP awards and/or the number of shares underlying unvested PSP awards, on the occurrence of a corporate event or other reorganisation.

In the event of a change of control, the treatment of long-term incentives will be determined in accordance with the relevant plan rules.

Maximum potential value

The maximum annual grant is 175% of base salary.

Performance measures

There are two performance measures which apply to PSP awards, as follows:

(i) **TSR** performance over three years relative to FTSE 350 comparator group (50% of award), vesting as follows:

Below Median = 0%
At Median = 25%
Upper Quartile = 100%

(ii) **Average corporate scorecard** (as described in the annual bonus) over three financial years (50% of award), vesting as follows:

Average Score 0.75 = 0%
Average Score 1 = 50%
Average Score 1.5 = 100%

While each annual corporate score can range from zero to 2.0, the three-year average corporate score is capped at 1.5. For illustration:

Year 1 Score 1.8
Year 2 Score 0.9
Year 3 Score 1.2
Average corporate score = 1.3

Straight line vesting occurs between performance levels for both conditions.

Pension
Pension provision is one of the components to attract, reward and retain the right calibre of executive, to ensure delivery of the leadership and management needed to execute the Group's vision and Business Plan.

Practical operation
Executive directors are entitled to non-contributory membership of the Group's defined contribution pension plan. The employer's contribution for executive directors is 20% of base salary.

Alternatively, at their option, executive directors may either have contributions of the same amounts made to their personal pension schemes, cash in lieu of pension (subject to normal statutory deductions); or a combination of pension contributions and cash in lieu of pension.

Maximum potential value
Maximum is 20% of base salary.

Performance measures
No performance measures apply.

Benefits
Benefits are provided to be market competitive as an integral part of directors' total remuneration.

Practical operation
Executive directors receive a car allowance, life assurance (four times salary), the opportunity to participate in all-employee share plans on the same basis as other employees, annual private health assessment and annual private medical cover.

Additional benefits may be provided if the Committee considers them appropriate.

Relocation expenses and/or second base expenses are paid, where appropriate, in individual cases. Directors' relocation expenses are determined on a case-by-case basis. The policy is designed to assist the director to relocate to a home of similar standing.

Maximum potential value
Benefits are set at a level appropriate to the individual's role and circumstances.

The maximum opportunity will depend on the type of benefit and cost of its provision, which will vary according to the market and individual circumstances.

Performance measures
No performance measures apply.

Share ownership guideline
The Group's share ownership guidelines align the interests of executives with shareholders.

Practical operation
The share ownership guideline is that all executive directors should retain shares to the value of 200% of base salary, to be accumulated over five years. Until this level is reached, directors who receive shares by virtue of any share plan award or who receive deferred bonus shares must retain 50% of the shares received net (i.e. after income tax and national insurance contributions). Only shares that have actually vested count towards the threshold.

Maximum potential value
N/A

Performance measures
N/A

Changes to executive directors' remuneration policy from previous policy

A summary of the key changes to the existing Drax remuneration policy approved by shareholders at the 2014 AGM (the existing policy) is set out below:

Component	Existing policy	New policy	Reasons for change
Base salary	Where an executive director has been appointed at a starting salary below market, the director's salary may be increased to market, but increases in any one year are limited to not more than 5% above the average for the workforce in that year.	Removal of restriction for executive directors internally appointed below market salary or promoted to a role with increased scope or expanded nature of responsibilities.	Removing the limitations on salary increases in respect of internal promotions supports succession planning and encourages development of our talent pool.
Benefits and pensions	Changes to clarify operation and maximum value of benefits in existing policy.		N/A
Annual bonus	Executive directors with "good leaver" status receive their deferred shares, pro-rated for the period of service, immediately on cessation of employment.	New Deferred Share Plan introduced as vehicle for deferred element of bonus (remains as 35% of bonus earned). Deferred bonus shares for "good leavers" will vest in full without time pro-rating, at the normal vesting date.	Changes recognise that the primary aim of bonus deferral is to ensure that the short-term performance is linked to sustainable returns to shareholders, more closely aligning executives and shareholder interests.
Long-term incentives	BMP operated, whereby maximum opportunity is linked to annual bonus outcome. Maximum opportunity: Group Chief Executive – 225% of base salary, other executive directors – 210% of base salary. 50% based on relative TSR vs FTSE 51–150, with 15% vesting at median performance. 50% based on Company Scorecard with: – Nil vesting below a Score of 1 – 15% vesting for a Score of 1 – 100% vesting for a Score of 1.5 Awards released after three years.	Removal of link between annual bonus and long-term incentive opportunity and introduction of new Performance Share Plan. Maximum opportunity – 175% of base salary for all executive directors. 50% based on relative TSR vs FTSE 350 with 25% vesting at median performance. 50% based on Company Scorecard with: – Nil vesting below a Score of 0.75 – 50% vesting for a Score of 1 – 100% vesting for a Score of 1.5 Two-year holding period added post-vesting.	De-coupling the long-term incentives from the annual bonus simplifies remuneration. Increasing the vesting for achieving median TSR performance and a Company Scorecard of 1 achieves a better balance between performance and reward and aligns more closely with market norms. The change to the TSR comparator group reflects Drax's market capitalisation. Introduction of holding period aligns executives more closely with shareholder value over the longer term and brings the operation more in line with corporate governance best practice.
Shareholding requirement	Shareholding of 175% of base salary for the Group Chief Executive and 125% of base salary for other executive directors to be accumulated.	Shareholding of 200% of base salary to be accumulated for all executive directors within a five-year period.	Further strengthening the alignment of executive and shareholder interests. Equalisation of shareholding requirements across the executive directors is in line with our team approach to executive remuneration.

Elements of existing policy that will continue – BMP awards made in 2014, 2015 and 2016

Remuneration component and link to strategy	Practical operation	Performance measures
Bonus Matching Plan – deferred and conditional awards made in 2014, 2015 and 2016. Links long-term share-based incentives to TSR and to the achievement of Business Plan strategic targets.	Vesting is subject to the achievement of performance conditions (conditional awards) and continued service or "good leaver" termination provisions (deferred and conditional awards). Further details of the terms of the awards were included in the Annual remuneration reports of the respective years.	Vesting of conditional awards is subject to relative TSR and average corporate scorecard outcome over three years.

Performance measures and approach to setting targets

The measures for elements of variable pay are:

- Corporate scorecard, consisting of strategic and Business Plan targets set by the Committee each year in conjunction with the Board. The corporate scorecard aligns incentives of executive directors with achievement of key business goals.
- Personal objectives, which typically reflect the collective performance of the executive directors in providing effective day-to-day leadership of the Group, as a unified leadership team.
- Relative TSR, which aligns executive director remuneration with creation of long-term shareholder value.

The Committee sets targets for the performance measures each year, taking into account market conditions, the Business Plan and other circumstances as appropriate. A summary of the corporate scorecard targets that apply for the following year are disclosed in the Annual report on remuneration on page 105.

Circumstances in which malus or clawback may apply

Malus and/or clawback may be applied to incentive awards under the following circumstances:

- **Clawback for the annual bonus** – the Committee may require a director to repay any amount of annual bonus payment it considers appropriate, in circumstances of financial misstatement, or misconduct, or if assessment of a performance condition is found to have been based on an error, inaccuracy or misleading information, or in other circumstances that the Committee considers to justify the operation of the clawback provision.
- **Malus and clawback for the BMP** – if a repayment of bonus is required (see "annual bonus" above) the Committee shall reduce the number of shares that may vest under the BMP by an appropriate amount (in respect of an award made pursuant to the annual bonus payment subject to the clawback). The Committee may also reduce the number of shares under a BMP award in circumstances of financial misstatement, or if assessment of a performance condition is found to have been based on an error, inaccuracy or misleading information, or in other circumstances that the Committee considers to justify the operation of the clawback provision.
- **Malus and clawback for the PSP and DSP** – the Committee may also reduce the number of shares under a PSP and/or DSP award in circumstances of financial misstatement, or if assessment of a performance condition is found to have been based on an error, inaccuracy or misleading information, or in other circumstances that the Committee considers to justify the operation of the clawback provision.

Committee's judgement and discretion

In addition to assessing and making judgements on the meeting of performance targets and the appropriate incentives payable, the Committee has certain operational discretions it can exercise in relation to executive directors' remuneration. These include, but are not limited to:

- reviewing the formulaic outcome of the annual bonus and applying discretion to amend the final outcome, to ensure that bonus payments reflect overall performance;
- deciding whether to apply malus or clawback to an award; and
- determining whether a leaver is a "good leaver".

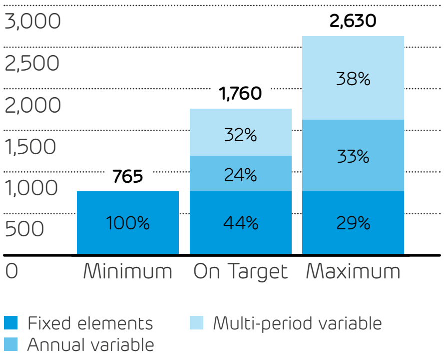
Where such discretion is exercised, it will be explained in the relevant directors' remuneration report.

Remuneration scenarios

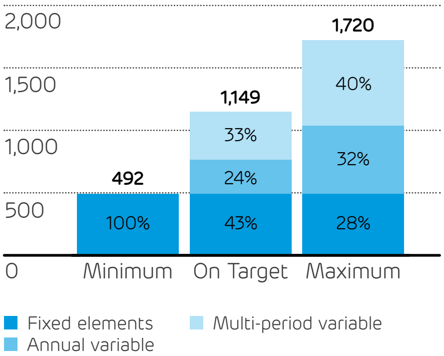
The composition and value of the executive directors' remuneration packages at threshold, target and outperformance scenarios under the Drax Group remuneration policy are set out in the charts below. The assumptions used in the charts are provided in the following table:

Scenario	Base salary, pension and benefits	Annual bonus	PSP
Minimum	Salary is the rate payable to each director from 1 January 2017	None	None
Target	The value of benefits is taken from the single figure for the year ended 31 December 2016	50% of the maximum bonus	TSR: 62.5% vesting (midpoint between threshold and maximum) Scorecard: 50% vesting
Maximum	Pension is the value of the pension payable on the salary rate used	Maximum bonus (150% of salary for Group Chief Executive, 140% of salary for other executive directors)	Maximum PSP opportunity (175% of salary) with no allowance for share price appreciation or dividend equivalents

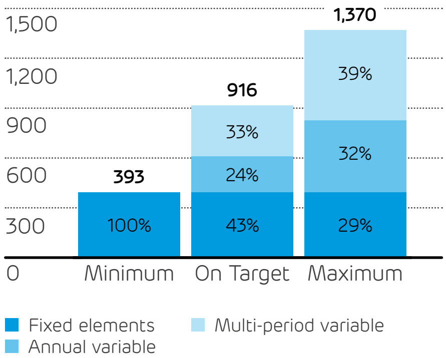
Dorothy Thompson (Chief Executive, Drax Group) Remuneration £000s



Will Gardiner (Chief Financial Officer) Remuneration £000s



Andy Koss (Chief Executive, Drax Power) Remuneration £000s



Approach to recruitment remuneration

The Committee will apply the core principles on page 84 and the components set out in the table on pages 86 to 89 to determine the remuneration of newly appointed directors. Base salary will be set at a level appropriate to the role and the experience of the director being appointed. Where this is below the market level, it will be adjusted over time to align with the market level, subject to good performance. In relation to directors appointed from outside the Group, where the Committee considers it to be necessary to secure the appointment of the director, the Committee may:

– pay "sign-on" compensation for loss of benefits on resignation from a previous employer, such as loss of long-term share incentives (subject to the right to phase any payment to reflect performance, the requirement to mitigate loss and the Company's right to clawback any amount which is subsequently paid to the executive by the former employer, and to clawback an appropriate proportion of the payment if the executive leaves soon after appointment); and
– make appropriate payments in circumstances where a director is relocated from outside the UK.

Service agreements and compensation on loss of office

Executive directors' service agreements are of indefinite duration, terminable at any time by either party giving 12 months' notice.

Element	Details
Notice periods	Executive directors may be required to work during the notice period or may be provided with pay in lieu of notice if not required to work the full notice period. Under each of the executive directors' service agreements, the Company has the right to make a payment in lieu of notice of termination, the amount of that payment being the salary and benefits that would have accrued to the executive director during the contractual notice period.
Compensation for loss of office	If an executive director's employment is brought to an end by either party and if it is necessary to determine a termination payment, the Committee's policy, in the absence of a breach of the service agreement by the director, is to determine a director's termination payment in accordance with his/her service agreement. The termination payment will be calculated based on the value of base salary and contractual benefits that would have accrued to the director during the contractual notice period. The Committee will seek mitigation to reduce the amount of any termination payment to a leaving director when appropriate to do so, having regard to the circumstances and the law governing the agreement. It may, for example, be appropriate to consider mitigation if the director has secured another job at a similar level. Mitigation would not apply retrospectively to a contractual payment in lieu of notice. In addition, the director may be entitled to a payment in respect of his/her statutory rights. No service agreement includes any provision for the payment of compensation upon termination. Any compensation payable in those circumstances would need to be determined at the time and in the light of the circumstances.
Treatment of annual bonus on termination	All bonus payments are discretionary benefits. The Committee will consider whether a departing director should receive an annual bonus in respect of the financial year in which, and/or immediately preceding which, the termination occurs, pro-rated to reflect the period of the performance year completed at the date of termination. The Committee will take into account performance; cooperation with succession; any breach of goodwill, and adherence to contractual obligations/restrictions. If the termination is by the Company on less than the notice specified in the director's service agreement, the Committee will also consider whether the director should receive an annual bonus in respect of any period of the financial year following termination for which the director has been deprived of the opportunity to earn annual bonus. If the employment ends in any of the following circumstances, the director will be treated as a "good leaver" and the director will be eligible for a bonus payment: – redundancy; – retirement; – ill-health or disability, proved to the satisfaction of the Company; and – death. If the termination is for any other reason, a bonus payment will be at the Committee's discretion and it is the Committee's policy to ensure that any such bonus payment properly reflects the departing director's performance and behaviour towards the Company. Therefore the amount of any such payment will be determined as described in the table on page 87, taking into account (i) the director's personal performance and behaviour towards the Company and (ii) the Group performance. If a bonus payment is made, it will normally be paid as soon as is reasonably practicable after the Group performance element has been determined for the relevant period. There may be circumstances in which the Committee considers it appropriate for the bonus payment to be made earlier, for example, on termination due to ill-health, in which case, on-target Group performance score shall be assumed. No payment will be made unless the director is employed on the date of bonus payment, except for "good leavers" as defined above.
Treatment of unvested long-term incentive and deferred share awards on termination	The Committee will consider the extent to which deferred and conditional share awards held by the director under the BMP, DSP and PSP should lapse or vest. Any determination by the Committee will be in accordance with the rules of the BMP (as approved by shareholders), DSP and PSP. In summary, the rules of the BMP and PSP provide that awards will vest (pro-rated to the date of employment termination) if employment ends for any of the following reasons ("long-term good leaver reasons"): – redundancy; – retirement; – ill-health or disability proved to the satisfaction of the Company; – change of ownership; and – death. If employment ends for any other reason, the rules of the BMP and PSP require the Committee to exercise its discretion. In doing so, it will take account of all relevant circumstances, in particular, the Company's performance; the director's performance and behaviour towards the Company during the performance cycle of the relevant awards; and other relevant factors, including the proximity of the award to its maturity date. The rules of the BMP also provide that in circumstances where awards vest, deferred and conditional shares vest as soon as reasonably practicable following termination. Awards, which vest subject to satisfaction of the relevant performance conditions, will be time pro-rated and will be phased over the performance cycle of the relevant awards. The rules of the DSP provide that deferred bonus awards will vest (in full) if employment ends for any of the long-term "good leaver" reasons detailed above. If employment ends for any other reason, the rules of the DSP require the Committee to exercise its discretion. In doing so it will take account of all relevant circumstances, in particular, the Company's performance; the director's performance and behaviour towards the Company during the performance cycle of the relevant awards; and a range of other relevant factors, including the proximity of the award to its maturity date. The rules of the DSP and PSP also provide that in circumstances where awards vest, they do so at the normal vesting date, unless the Committee exercises discretion to vest awards earlier. Awards which vest subject to satisfaction of the relevant performance conditions will be (time) pro-rated.
Outside appointments	Executive directors may accept external Board appointments, subject to the Chairman's approval. Normally only one appointment to a listed company would be approved. Fees may be retained by the director.

Consideration of circumstances for leavers

The Committee will consider whether the overall value of any benefits accruing to a leaving director is fair and appropriate, taking account of all relevant circumstances. Examples of circumstances in which the Committee may be minded to award an annual bonus payment and/or permit the vesting of PSP awards include:

- the director's continued good performance up to and following the giving of notice; and
- the director accommodating the Company in the timing of his/her departure and handover arrangements.

Conversely, the Committee may be minded not to allow such payments if the reason for the departure is:

- poor performance; or
- the director does not continue to perform effectively following notice.

Remuneration of non-executive directors and Chairman

Remuneration component and link to strategy	Practical operation	Maximum potential value
Fees To attract a Chairman and independent non-executive directors who, together with the executive directors, form a Board with a broad range of skills and experience.	The Chairman's remuneration is determined by the Committee whilst that of the other non-executive directors is determined by the Chairman and the executive directors. These are determined in the light of: – fees of chairmen and non-executive directors of other listed companies selected for comparator purposes, on the same basis as for executive directors; – the responsibilities and time commitment; and – the need to attract and retain individuals with the necessary skills and experience. Non-executive directors' fees are reviewed periodically against market comparators. They were last reviewed in 2016. Current fee levels are shown in the annual report on remuneration. The Chairman receives an annual fee. Non-executive directors receive an annual base fee. Additional annual fees are paid: – to the Senior Independent Director (which includes the fee for chairing a Board Committee other than the Audit Committee); – to the Chair of the Audit Committee; – to the Chair of the Remuneration Committee; and – to the Chair of any other Committee (this is not paid to the Chairman of the Nominations Committee if he or she is also the Chairman of the Board). Non-executive directors are not entitled to participate in any performance related remuneration arrangements.	Overall aggregate fees paid to all non-executive directors will remain within the limit as stated in the Company's Articles (currently £1,000,000).
Expenses	Reasonable travel and accommodation expenses are reimbursed as applicable.	

Non-executive directors do not receive any benefits in kind, nor are they eligible for any annual performance bonus, pension or any of the Group's share-based reward plans.

The Chairman's notice period is six months whilst the other non-executive directors have a notice period of one month.

Differences between the policy and that of the remuneration of employees generally

The following differences apply between the remuneration of directors and the policy on the remuneration of employees generally:

- executive directors and a number of senior employees are eligible for PSP awards, however, there are differences in terms of levels of grant;
- annual bonus levels vary across the workforce, and the requirement to defer a portion of annual bonus applies only to executive directors;
- employees in the collective bargaining unit have a contractual right to receive an annual bonus subject to Company performance and continued employment, whereas directors and all other UK-based employees participate in a discretionary bonus scheme; and
- hourly paid employees qualify for overtime payments.

Context

Wider employee population

In determining executive remuneration, the Committee also takes into account the level of general pay increases within the Group.

The Committee's policy is that annual salary increases for executive directors should not exceed the average annual salary increase for the wider employee population, unless there is a particular reason for a higher increase, such as a change in the nature or scope of responsibilities or if an executive director has been appointed at a salary below market level reflecting experience in the role.

The Committee has considered a number of comparison metrics when determining its approach to executive remuneration, including the ratio of Group Chief Executive to median employee pay. The Committee considered that the ratio is appropriate, particularly as the majority of the Group Chief Executive's pay is performance linked.

Views taken from the employee population

In the course of discussions on pay with employee representatives, the Group discusses executive remuneration policy and provides details of the process by which the Committee establishes executive remuneration packages. The information provided includes details of the benchmarking of executive director remuneration, as well as information benchmarking the pay of employees in the collective bargaining unit with pay elsewhere in the industry.

Environmental, social and governance issues

The Committee is able to consider corporate performance on environmental, social and governance issues when setting the remuneration of executive directors. Specific measures can be included in the balanced corporate scorecard. The Committee is also able to consider these issues in determining whether to exercise its discretion to adjust the overall score, and in considering the performance conditions override under the PSP, as described on page 88.

Shareholder engagement

The Company holds regular meetings with its largest shareholders, and the Committee takes into account any shareholder views or representations relating to executive remuneration. The Company has consulted its 12 largest shareholders in relation to the formulation of its new directors' remuneration policy.

Annual report on remuneration

The relevant sections of this report have been audited as required by the Regulations.

Single total figure of remuneration for each director (audited information)

The table below sets out the single figure of remuneration and the breakdown for each executive director for 2016, together with comparative figures for 2015:

	Salary/Fees (£000)		Pension (£000)		Bonus[1] (£000)		BMP[2] (£000)		Other benefits (£000)		Total (£000)	
Name	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015
Dorothy Thompson	**574**	571	**115**	114	**756**	393	**60**	96	**76**	74	**1,581**	1,248
Will Gardiner[3]	**390**	49	**78**	10	**479**	34	**–**	–	**24**	3	**971**	96
Andy Koss[4]	**310**	n/a	**62**	n/a	**381**	n/a	**16**	n/a	**21**	n/a	**790**	n/a

Notes:
(1) Bonus is the cash value of the annual bonus payable in respect of performance in the relevant year, including the value of bonus deferred and paid in shares after three years subject only to continued service.
(2) BMP is the value of the BMP Matching Awards vesting in March 2017, together with the dividend shares in relation to those vested shares. The value is calculated based on the average share price over the last quarter of 2016.
(3) Will Gardiner was appointed as a director on 16 November 2015.
(4) Andy Koss was appointed as a director on 1 January 2016.

Base salaries

The base salaries of the executive directors as at 31 December 2016, together with comparative figures as at 31 December 2015, are shown in the following table:

	Base salary as at 31 December 2016 £000	Base salary as at 31 December 2015 £000	Percentage increase
Andy Koss[1]	**310**	n/a	n/a
Will Gardiner	**390**	390	0%
Dorothy Thompson	**574**	574	0%

Note:
(1) Andy Koss was appointed as a director on 1 January 2016.

Annual fees

The Chairman's fee was set at £250,000 on his appointment on 22 April 2015 and the fee was reviewed on 16 September 2016. Non-executive directors' fees were last reviewed on 1 August 2015. Fee rates as at 31 December 2016 and 31 December 2015 are shown in the following table:

	Fees at 31 December 2016 £000	Fees at 31 December 2015 £000	Percentage increase
Chairman	**250**	250	0%
Non-Executive Director base fee	**55**	55	0%
Senior Independent Director	**10**	10	0%
Audit Committee Chair	**10**	10	0%
Remuneration Committee Chair	**10**	10	0%
Nominations Committee Chair[1]	**7.5**	7.5	0%

Note:
(1) This is not paid if the Chairman of the Nominations Committee is also the Chairman of the Board.

The table below sets out the single figure of remuneration and breakdown for each non-executive director for 2016 together with comparative figures for 2015:

	Board fee (£000)		Other fees (£000)		Total (£000)	
	2016	2015	**2016**	2015	**2016**	2015
Philip Cox						
Chairman of Board	**250**	190	**–**	–	**250**	190
Chairman of Nominations Committee						
Tim Cobbold	**55**	55	**–**	–	**55**	55
Melanie Gee(1)	**17**	55	**–**	–	**17**	55
David Lindsell	**55**	55				
Senior Independent Director			**10**	10		
Chairman of Audit Committee			**10**	10	**75**	75
Tony Thorne	**55**	55				
Chairman of Remuneration Committee			**10**	10	**65**	65

Note:
(1) Melanie Gee retired as a director of the Board at the conclusion of the AGM on 20 April 2016. She received her annual fee pro-rated to her date of leaving.

Details of performance against metrics for variable pay awards

Annual bonus plan outcome

A summary of the Committee's assessment in respect of the 2016 Scorecard is set out in the following table:

	Target weighting	Low target	Target	Stretch target	Outturn	Score
Group – Corporate						
Safety						
Total recordable injury rate	5%	0.70	0.30	0.15	0.22	1.5
Finance						
Group underlying earnings per share (pence)	10%	0.0	1.1	5.9	5.0	1.8
Group underlying EBITDA (£m)	10%	125	130	149	140	1.5
Cash balance at 31 December	10%	145	149	164	228.5	2.0
Group operating costs (£m)	10%	248	238	218	236.3	1.1
Regulation						
EU state aid approval of CfD	20%	Late approval with conditionality	Timely approval no conditions	Early approval, no conditions	Close to target	0.9
General						
Increasing support for Group's business activities through media channels [1]	5%	Consolidated score – significantly unfavourable	Consolidated score – favourable	Consolidated score – significantly favourable	Above target	1.3
Drax Biomass						
Availability H2	5%	Significantly below target	At target	Significantly above target	Below target	0.2
Pellet quality H2[2]	5%	Significantly below target	At target	Significantly above target	Above target	1.1
Drax Power						
Value from operational flexibility and system support[3]	5%	£25m	£37m	£47m	£62m	2.0
Progress in further coal unit conversions	5%	None	Executable options	Advanced progress	Viable engineering options developed	0.5
Retail (Haven/BBE)						
Margin improvement initiatives (MI) in 2016[4]	5%	£1m	£2m	£3m	£3m	2.0
Renewable sales at a premium	5%	Significantly below target performance	On target performance	Significantly above target performance	Above target	1.2
Total weighting	100%					1.3

Notes:
(1) Based on external assessment of media reports.
(2) Pellet quality combines calorific value, fines content at port and durability.
(3) Combined gross margin from using fuel optionality and generation flexibility and reliability.
(4) Management initiatives to improve margins and profitability without risking volume or cash.

Further details of how these individual metrics support the business strategy and drive both shareholder value and performance are found on pages 1 to 61.

The Committee made an in-depth review of the score for each of the performance measures, to make sure these were individually supportable, and then reviewed the overall outcome, to determine whether to exercise its discretion and adjust the final score. The majority of the measures are quantitative but for reasons of commercial sensitivity some of the targets are not disclosed in the Annual report. The Committee aims for maximum transparency so the decision not to disclose a target is closely reviewed. 50% of the measures were financial and some 50% related to the implementation of the strategy. Outlined below is a brief synopsis of the key strategic measures and their strategic rationale.

Regulation: Securing the CfD – supports biomass conversion and improves predictability of revenues;
General: Increasing support for Group's activities – secure sustainability of biomass as a valued renewable technology;
Drax Biomass: availability and quality – develop strong in-house pellet supply capability;
Drax Power: value from operational flexibility – build sustained earnings from system support; progress in further coal unit conversion – create option for further conversion to biomass;
Retail Haven: renewable sales at a premium – increase proportion of renewable power, in support of Group strategy.

Personal performance
The members of the Executive Committee, including the executive directors were assessed both relative to their individual contribution in driving 2016 performance, and as a team. Key to the assessment was each individual's contribution to delivering the Group's strategy and promotion of the Drax values. Individual and team performance were both considered to be at a high level.

There was good cooperation across the executive team, which was fundamental to the successful development and implementation of the mitigating actions in response to the challenging commodity markets and the European Commission delay in the approval of the CfD. The Committee also recognised the collaborative approach to the development and implementation of the new strategy.

With respect to the executive directors areas of particular note included:

- the Group Chief Executive's strong and effective leadership of the Group, the work on sustainability and the development, promotion and implementation of the new strategy, which included two significant acquisitions;
- the Chief Financial Officer's success in identifying and implementing efficient and effective solutions for the Group's capital structure, his good support of the Group Chief Executive in the development and implementation of the new Group strategy, including responsibility for the IT strategy, the analysis of new opportunities and their potential fit to Drax and his leadership of the Opus acquisition, including the financing arrangements;
- the Chief Executive of Drax Power's strong leadership of the Drax generating plant, completion of the biomass transformation through the conversion of the third unit, the significant revenue initiatives within ancillary services, the work on the CfD and the leadership of the acquisition of the four development projects to build fast response gas plants.

The Committee determined that the three executive directors had performed strongly and that it was appropriate to give the same personal performance score to each. A score of 1.35 out of 1.5 was awarded.

Actual bonus awards for 2016

Executive director	Value of bonus[1] £000	2016 bonus payment (as a % of base salary)
Dorothy Thompson, Chief Executive, Drax Group	756	132%
Will Gardiner, Chief Financial Officer	479	123%
Andy Koss, Chief Executive, Drax Power	381	123%

Notes:
(1) The value of the bonus shown in the table above is made up of 65% paid in cash and 35% deferred into shares.

Details of deferred bonus share awards (audited information)
The following deferred bonus shares, which were awarded in 2013 in respect of the 2012 annual bonus, vested in 2016.

Executive director	Value of vesting[1] £000	Number of shares
Dorothy Thompson, Chief Executive, Drax Group	80	29,494

Notes:
(1) The value of the vesting is based on the share price (270.27 pence) at which the shares were subject to income tax and National Insurance Contributions on the vesting date.
(2) Paul Taylor ceased to be a director on 31 December 2015 but remained an employee. His deferred bonus shares awarded in 2013 in respect of the 2012 annual bonus vested in 2016. The total number of shares which vested from those awards (including dividend shares) was 12,810 and the value of the vesting was £34,622, which was based on the share price (270.27 pence) at which the shares were subject to income tax and National Insurance Contributions on the vesting date.

Detail of BMP incentive outcomes (audited information)
Awards under the BMP, which were subject to performance conditions and which vested in 2016, were:

- TSR performance condition: 0%
- Scorecard performance condition: 43.33%

Directors' interests under the BMP
The table below shows the interests of the executive directors in the Company's BMP, as at 31 December 2016 and 15 February 2017.

	As at 1 January 2016	Awards made during the year	Awards vesting during the year	Awards lapsing during the year	**As at 31 December 2016**	Face value of awards (£)
Dorothy Thompson						
2013 Matching Award	162,146	–	35,128	127,018	**–**	–
2013 Deferred Award	27,024	–	27,024	–	**–**	–
Dividend shares awarded	–	5,682	5,682	–	**–**	–
2014 Matching Award	131,425	–	–	–	**131,425**	£496,655
2014 Deferred Award	21,904	–	–	–	**21,904**	£82,775
2015 Matching Award	225,958	–	–	–	**225,958**	£853,895
2015 Deferred Award	52,723	–	–	–	**52,723**	£199,240
2016 Matching Award	–	254,183	–	–	**254,183**	£960,558
2016 Deferred Award	–	59,309	–	–	**59,309**	£224,129
Total	**621,180**	**319,174**	**67,834**	**127,018**	**745,502**	**£2,817,252**
Will Gardiner						
2016 Matching Award	–	353,504	–	–	**353,504**	£1,335,891
2016 Deferred Award	–	5,063	–	–	**5,063**	£19,133
Total	**–**	**358,567**	**–**	**–**	**358,567**	**£1,355,024**
Andy Koss						
2013 Matching Award	26,512	–	5,743	20,769	**–**	–
2014 Matching Award	33,982	–	–	–	**33,982**	£128,417
2015 Matching Award	49,160	–	–	–	**49,1601**	£185,775
2016 Matching Award	–	61,999	–	–	**61,999**	£234,294
Total	**109,654**	**61,999**	**5,743**	**20,769**	**145,141**	**£548,486**

Notes:
(1) In accordance with the BMP rules, dividend shares are only awarded, at the time and in the event that, awards actually vest. No dividend shares are awarded where the initial awards lapse. The number of dividend shares awarded is calculated based on the actual dividends paid to ordinary shareholders in the period following the initial award up until the award vests.
(2) The Deferred Awards referred to above are the share awards made in respect of the deferral of cash bonus awarded each year. Those share awards operate under the rules of the BMP.
(3) Details of the conditions subject to which the above awards will vest are given on page 91.
(4) The face value of the awards is calculated based on the share price on 31 December 2016, which was 377.9 pence per share.

The table below shows former directors' interests in the Company's BMP, as at 31 December 2016 and 15 February 2017.

	As at 1 January 2016	Awards made during the year	Awards vesting during the year	Awards lapsing during the year	**As at 31 December 2016**	Face value of awards (£)
Peter Emery(5)						
2013 Matching Award	83,817	–	17,197	66,620	**–**	–
2013 Deferred Award	13,970	–	13,230	740	**–**	–
Dividend shares awarded	–	2,778	–	–	**–**	–
2014 Matching Award	67,936	–	–	–	**67,936**	£256,730
2014 Deferred Award	11,322	–	6,952	4,370	**–**	–
2014 Dividend shares awarded	–	–	–	–	**–**	–
2015 Matching Award	123,833	–	–	–	**123,833**	£467,964
2015 Deferred Award	28,894	–	7,961	20,933	**–**	–
2015 Dividend shares awarded	–	–	–	–	**–**	–
Total	**329,772**	**2,778**	**45,340**	**92,663**	**191,769**	**£724,694**
Paul Taylor(6)						
2013 Matching Award	70,434	–	15,259	55,175	**–**	–
2013 Deferred Award	11,739	–	11,739	–	**–**	–
Dividend shares awarded	–	2,465	2,465	–	**–**	–
2014 Matching Award	57,089	–	–	–	**57,089**	£215,739
2014 Deferred Award	9,514	–	–	–	**9,514**	£35,953
2015 Matching Award	104,062	–	–	–	**104,062**	£393,250
2015 Deferred Award	24,281	–	–	–	**24,281**	£91,757
2016 Matching Award	–	–	–	–	**–**	–
2016 Deferred Award	–	27,314	–	–	**27,314**	£103,219
Total	**277,119**	**29,779**	**29,463**	**55,175**	**222,260**	**£839,918**

Notes:
(1) In accordance with the BMP rules, dividend shares are only awarded at the time and in the event that, awards actually vest. No dividend shares are awarded where the initial awards lapse. The number of dividend shares awarded is calculated based on the actual dividends paid to ordinary shareholders in the period following the initial award up until the award vests.
(2) The Deferred Awards referred to above are the share awards made in respect of the deferral of cash bonus awarded each year. Those share awards operate under the rules of the BMP.
(3) Details of the conditions subject to which the above awards will vest are given on page 91.
(4) The face value of the awards is calculated based on the share price on 31 December 2016, which was 377.9 pence per share.
(5) Peter Emery left the Company on 31 December 2015. The Awards which vested were pro-rated from the date of the Award to the date of leaving.
(6) Paul Taylor ceased to be a director on 31 December 2015 but he has continued in employment on a part-time basis. Paul's 2016 BMP Award was in respect of his role as a director in 2015.

Total pension entitlements for defined contribution schemes (audited information)

Executive directors are entitled to non-contributory membership of the Group's defined contribution pension plan, with either an employer contribution of 20% of base salary, or contributions to a personal pension, or cash in lieu of pension, or a combination of any of these up to a maximum contribution of 20% of base salary.

No director was a member of the defined benefit pension scheme.

Payments for loss of office

Melanie Gee ceased to be a non-executive director on 20 April 2016, following her retirement at the conclusion of the AGM. In 2016, she received her annual base fee of £55,000 as a non-executive director, pro-rated for the period 1 January 2016 to her date of leaving. The actual fees received for the period were £16,805.

Peter Emery ceased to be a director of the Company on 31 December 2015 and his service agreement terminated on that date. In 2016 he received a payment of £183,737, which was in line with the provisions of his service agreement and the Company's remuneration policy as set out in this report. An initial payment of £183,737 in lieu of outstanding notice for the period 1 January 2016 to 10 November 2016 in respect of salary, pension payments and contractual benefits ("the PILON payment") was paid in January 2016 as the initial payment of 50% of the PILON payment. Any further instalments of the PILON payment will be calculated when the value of his remuneration from alternative employment can be determined.

Shareholder voting

The table below shows the voting outcome for the Remuneration Policy at the AGM on 23 April 2014 and for the Annual report on remuneration at the AGM on 20 April 2016.

	For		Against		Votes withheld		Total	
	Shares	(%)	Shares	(%)	Shares	(%)	Shares	(%)
Approval of the directors' remuneration policy (2014)	272,348,741	82.00	17,116,591	5.16	42,643,941	12.84	332,109,273	100
Approval of the annual report on remuneration	359,318,445	98.78	464,991	0.13	3,968,115	1.09	363,751,551	100

The new Remuneration Policy is subject to a shareholder vote at the 2017 AGM.

Statement of directors' shareholding and share interests (audited information)

During the year, the shareholding guidelines required executive directors who receive shares by virtue of share plan awards, or who receive deferred bonus shares, to retain 50% of the shares received net (i.e. after income tax and National Insurance Contributions) until the value was equal to at least 175% and 125% of salary respectively for the Group Chief Executive and other executive directors. Only shares that have actually vested count towards the threshold.

As at 31 December 2016, the shareholding guidelines were met in part, as detailed in the table below, which also shows the executive directors' shareholdings and share interests as at that date.

		Beneficial ownership of director or connected persons	Deferred Awards not subject to performance		Awards subject to performance	
Name	Year ending 31 December 2016	Shares[2]	BMP Share Awards[3]	Sharesave Options	BMP Share Awards	Total
Will Gardiner	Number	41,346	5,063	14,778	353,504	414,691
	Value at year end[1]	£156,247	£19,133	£55,846	£1,335,891	£1,567,117
	Shareholding as a percentage of salary	40%	–	–	–	–
Andy Koss	Number	34,153	–	5,633	145,141	184,927
	Value at year end[1]	£129,064	–	£21,287	£548,487	£698,839
	Shareholding as a percentage of salary	61%	–	–	–	–
Dorothy Thompson	Number	329,512	133,936	4,637	611,566	1,079,651
	Value at year end[1]	£1,245,225	£506,144	£17,523	£2,311,108	£4,080,001
	Shareholding as a percentage of salary	217%	–	–	–	–

Notes:
(1) Share price at 31 December 2016 was 377.9 pence per share.
(2) Includes, where applicable, shares held by the Trustee of the Drax Group plc Share Incentive Plan.
(3) The deferred share awards not subject to performance are the annual bonus deferred shares.

There is no shareholding requirement for non-executive directors. The table below shows the shareholdings of the non-executive directors and their connected persons and the value as at 31 December 2016, when the share price was 377.9 pence per share.

Name	Number of shares	Value at year end
Tim Cobbold	1,000	£3,779
Philip Cox	60,000	£226,740
David Lindsell	7,500	£28,342
Tony Thorne	7,500	£28,342

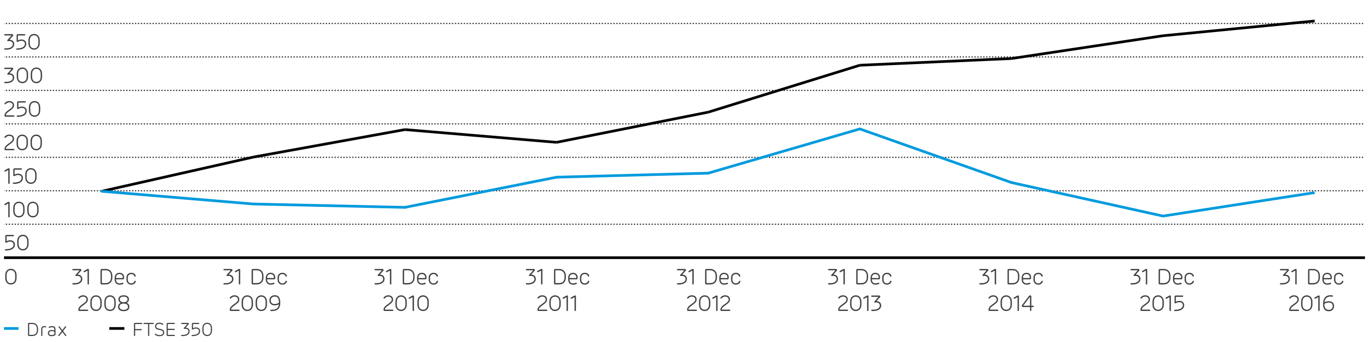
Service agreements

The following table shows, for each director of the Company at 15 February 2017, or those who served as a director of the Company at any time during the year ended 31 December 2016, the start date and term of the service agreement or contract for services, and details of the notice periods.

Director	Contract start date	Contract term (years)	Unexpired term at the date of publication (months)	Notice period by the Company (months)	Notice period by the director (months)
Tim Cobbold	27 September 2016	3 years	2 years and 7 months	1	1
Philip Cox	1 January 2015	3 years	10 months	6	6
Will Gardiner	16 November 2015	Indefinite term	Not applicable	12	12
Melanie Gee	1 January 2016	3 years	Not applicable	1	1
Andy Koss	1 January 2016	Indefinite term	Not applicable	12	12
David Lindsell	1 December 2014	3 years	9 months	1	1
Dorothy Thompson	3 September 2013	Indefinite term	Not applicable	12	12
Tony Thorne	29 June 2016	3 years	2 years and 4 months	1	1

Drax eight-year TSR data to 31 December 2016

The following graph shows how the value of £100 invested in both the Company and the FTSE 350 index on 31 December 2008 has changed. This index has been chosen as a suitable broad comparator against which the Company's shareholders may judge their relative returns given that, in recent years, the Company has been a member of the FTSE 350 index. The graph reflects the TSR (determined according to usual market practice) for the Company and the index referred to on a cumulative basis over the period from 31 December 2008 to 31 December 2016.



Group Chief Executive's pay in last eight financial years

Year	2009	2010	2011	2012	2013	2014	2015	**2016**
Dorothy Thompson's total single figure (£000)	903	1,155	1,196	1,406	3,360	1,854	1,248	**1,581**
Bonus % of maximum awarded	77%	100%	100%	100%	100%	73%	46%	**88%**
BMP Matching Award % of maximum vesting	–	–	–	–	–	40.52%	21.66%	**15.43%**

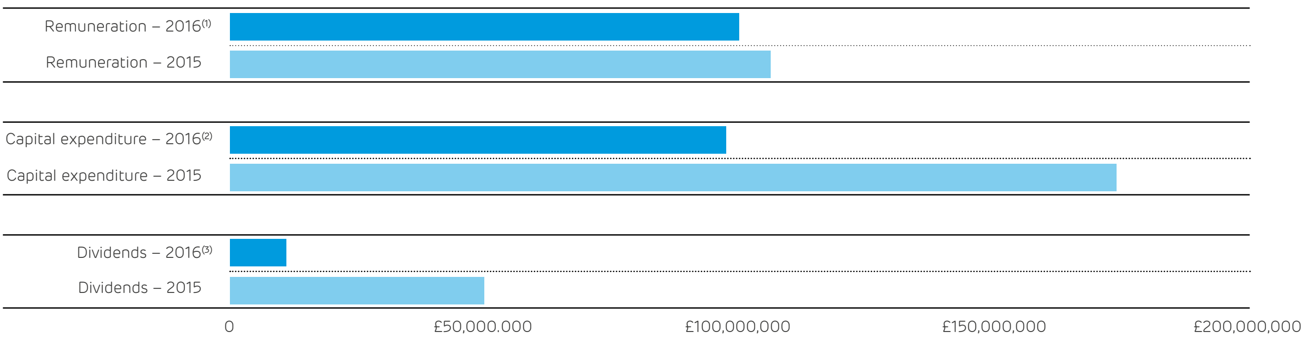
Percentage change in the Group Chief Executive's remuneration compared with the wider employee population

The table below shows how the percentage change in the Group Chief Executive's salary, benefits and bonus between 2015 and 2016 compares with the percentage change in the average of each of those components of pay for a group of employees. The Committee has selected all Group employees below executive director level based in the UK, as these are the vast majority of Group employees and provide the most appropriate comparator.

	Salary	Taxable benefits	Bonus		
			£000		
	Percentage increase	Percentage increase	2015	**2016**	% increase
Dorothy Thompson	0%	2.7%	392.6	**755.7**	92%
Average for UK employees	2.7%	0.7%	4.5	**6.6**	46%

Relative importance of spend on pay

The table below illustrates the relative importance of spend on pay compared to other disbursements from profit, namely distributions to shareholders and capital expenditure. These were the most significant outgoings from the Company in the last financial year, other than normal operating costs.



Notes:
(1) Remuneration 2016 see note 6.1.
(2) Capital expenditure 2016 see note 3.1.
(3) Dividends 2017 see note 2.7.

Statement of implementation of the Remuneration Policy in 2017

The Remuneration Policy will be implemented following the AGM in 2017 as follows:

The Committee will review salaries in accordance with the Policy and will take account of the increase in base pay of the collective bargaining group and other salary reviews in the Group.

Balanced corporate scorecard

The Scorecard measures and targets for 2017 have been established for the Group and for each Group business. Details of performance against the measures will be disclosed in the 2017 Annual report on remuneration so far as possible, whilst maintaining commercial confidentiality. The following table sets out the categories and a description of the measures.

Group	
Safety – Total recordable injury rate	Low target and stretch have both been set at the same level as 2016.
Finance – Group underlying earnings per share, profit, net debt	Targets take account of Business Plan and current market expectations.
Drax Biomass fines at UK disport	Strategic target based on optimising quality across the whole supply chain.
New strategy implementation	Progress in implementing new Group strategy and defined deliverables for identified projects as well as qualitative assessment of further progress.
Drax Biomass	
Variable costs	Targets for cost reduction $/tonne, Drax Biomass strategic focus: production of low cost pellets at quality.
Output	Target for reliable production – Drax Biomass strategic focus: sustained reliable operations.
Drax Power	
Biomass unit technical availability performance	Target for high availability – Drax Power strategic focus: maximise sustained value through availability.
Value from operational flexibility and reliability	Target to capture value from system support – Drax Power strategic focus: sustained earnings from system support given increase in UK electricity system stress.
Haven Power	
Profit	Target based on Business Plan – Haven strategic focus: sustained profitable business at scale.
Implementation of new ERP	Target based on detailed planned deliverables – Haven strategic focus: project delivery critical for strategy of achieving sustained profitability.
Opus	
Profit	Target based on Business Plan – strategic focus: delivering value from acquisition.
Sales volume	Target based on Business Plan – strategic focus: delivering continued growth at Opus.
Renewal rate	Target based on Business Plan – strategic focus: continued customer satisfaction to support growth and profitability.

Performance measures for Performance Share Plan

The performance measures to be used in 2017 PSP Awards are as described on page 88 in the Remuneration Policy report.

Non-executive directors' fees

Non-executive directors' fees will be reviewed by the Chairman and executive directors in July 2017.

Committee activity and key decisions in 2016
Matters considered and decisions reached by the Committee in 2016 are shown in the table below:

February	Considered the 2015 balanced corporate scorecard and decided not to exercise its discretion to adjust the score.
	Adopted the 2016 balanced corporate scorecard for the purpose of determining relevant aspects of 2016 remuneration.
	Approved executive director and senior staff personal scores and annual bonus awards for 2015.
	Approved the Group Chief Executive's annual bonus.
	Approved the vesting of the 2013 BMP awards, which was reported in the 2016 Annual report on remuneration.
	Considered succession planning.
	Considered the pro-rating of deferred bonus awards.
	Considered and approved the 2015 Annual Remuneration report.
	Approved awards under the BMP and all-employee Sharesave Share Plan.
	Approved the proposed approach and outline timetable for the review of the Remuneration Policy in preparation for its presentation to the 2017 AGM for approval.
March	Approved the retention of PwC as Remuneration Committee adviser.
	Considered a proposal for senior staff and executive directors' salary review.
	Considered the Remuneration Policy review.
June	Considered the Remuneration Policy review.
	Agreed the remuneration terms for Jonathan Kini's appointment to the Executive Committee.
	Considered the detail of the payments in respect of Peter Emery's payment in lieu of notice (PILON) payment.
September	Reviewed the Chairman's remuneration.
	Considered the Remuneration Policy review.
November	Noted the performance status of outstanding share plans and approved in principle the operation of share plans in 2017.
	Reviewed the fees paid to PwC as, the Committee's remuneration adviser, together with fees paid by the Group to PwC for other matters, and reviewed PwC's independence.

In 2016, the Remuneration Committee comprised Tony Thorne, Chairman of the Committee; Tim Cobbold; Philip Cox; David Lindsell; and Melanie Gee (until 20 April 2016), all of whom are independent non-executive directors. The Group Company Secretary acted as Secretary to the Committee.

The Group Chief Executive was invited to attend meetings of the Committee, except when her own remuneration was discussed.

The Committee met on five occasions during the year and its members' attendance record is set out on page 82, along with details of other attendees.

Adviser to the Committee
The adviser to the Committee for the year was PricewaterhouseCoopers LLP (PwC). PwC is an independent adviser appointed by the Committee in October 2010, following a competitive tender process, to advise on market practice and remuneration of executive and non-executive directors.

From time to time the Group engages PwC to provide financial, taxation and related advice on specific matters. The Committee will continue to monitor such engagements in order to be satisfied that they do not affect PwC's independence as an adviser to the Committee.

PwC was paid £78,000 during 2016 in respect of advice given to the Committee.

The Committee also considers the views of the Group Chief Executive regarding the performance and remuneration of the other executive directors and senior staff.

During 2016, the Committee has also been advised by Philip Hudson, the Group Company Secretary (to 30 June 2016), David McCallum, the Group Company Secretary (from 1 July 2016), Richard Neville, Head of Human Resources (to 31 July 2016) and Samantha Brook, Head of Corporate HR (from 1 August 2016).

Other matters

Wider employee population

The average pensionable pay of an executive director is 9.6 times the average of pensionable pay for all UK employees within the Group.

Remuneration received from external appointments

Remuneration received by executive directors for service as a non-executive director elsewhere is retained by the director. Detailed below is the remuneration they received.

Name	External organisation	Fees received 2015	Fees received 2016
Dorothy Thompson	Johnson Matthey Plc (resigned 20 July 2016)	£76,000	**£43,000**
Dorothy Thompson	Court of the Bank of England	£15,000	**£15,000**
Dorothy Thompson	Eaton Corporation plc (appointed 29 July 2016)	–	**£58,000**
Will Gardiner	Qardio plc	–	**–**

This report was reviewed and approved by the Remuneration Committee on 15 February 2017.

Tony Thorne
Chairman of the Remuneration Committee

DIRECTORS' REPORT

This report contains information which the Company is obliged to disclose and which cannot be found in the strategic, financial, sustainability or corporate governance reports of this document.

The directors present their annual report on the affairs of the Group, together with the financial statements and auditor's report for the year ended 31 December 2016. The Corporate governance section, Audit, Nominations and Remuneration Committee reports set out on pages 62 to 107 form part of this report.

No significant events have arisen since the balance sheet date. An indication of likely future developments in the business of the Company and details of research and development activities are included in the Strategic report on pages 1 to 61.

Information about the use of financial instruments by the Company and its subsidiaries is given in note 7.2 to the consolidated financial statements.

Annual General Meeting (AGM)

The AGM will be held at 11.30am on Thursday 13 April 2017 at The Grand Hotel and Spa, Station Rise, York, YO1 6GD. A separate document contains the notice convening the AGM and includes an explanation of the business to be conducted at the meeting.

Dividends

An interim dividend of 2.1 pence per share was paid on 7 October 2016, to shareholders on the register on 23 September 2016.

The directors propose a final dividend of 0.4 pence per share, which will, subject to approval by shareholders at the AGM, be paid on 12 May 2017, to shareholders on the register on 21 April 2017.

Details of past dividends can be found on the Company's website at http://www.drax.com/investors/financial-history/#dividend-history/

No shareholder has waived or agreed to waive dividends payable in the year or in future years.

Share capital

The Company has only one class of equity shares, which are ordinary shares of $11^{16}/_{29}$ pence each. There are no restrictions on the voting rights of the ordinary shares.

Drax Group plc has a Premium Listing on the London Stock Exchange and currently trades as part of the FTSE 250 Index, under the symbol DRX and with the ISIN number GB00B1VNSX38.

Shares in issue

At 1 January 2016	**406,317,162**
Issued in period through the Bonus Matching Plan(1)	365,937
Issued in period through the Sharesave Plan(2)	17,222
At 31 December 2016	**406,700,321**
Issued between 1 January and 14 February 2017 through the Sharesave Plan	**2,216**
At 14 February 2017	**406,702,537**

Notes:
(1) 103 members of the Bonus Matching Plan had shares vest at the third anniversary following the Award and one employee had Deferred Awards vest upon leaving the Company.
(2) Two members of the Sharesave Plan exercised options at the maturity of their 2011 five-year grant, and seven members exercised their options early upon retirement or redundancy.

No other ordinary shares were issued during the year and the Company held no treasury shares during 2016. The position remains the same at the date of this report.

Interests in voting rights

Information provided to the Company in accordance with the Financial Conduct Authority's Disclosure and Transparency Rules (DTR) is published in a timely manner on the London Stock Exchange's Regulatory News Service – a Regulatory Information Service and also on the Company's website.

As at 15 February 2017, the following information had been received in accordance with DTR5 from holders of notifiable interests in the voting rights of the Company. The information provided below was correct at the date of notification. However, investors are only obliged to notify the Company when a notifiable threshold is crossed and therefore it should be noted that the holdings below may have changed but without crossing a threshold.

	Date last notification made	Number of voting rights directly held	Number of voting rights indirectly held	Number of voting rights in qualifying financial instruments	Total number of voting rights held	% of the issued share capital held(2)
Invesco plc(1)	10.01.2017	–	89,210,833	–	89,210,833	21.93%
Schroders plc	09.12.2016	–	62,338,377	–	62,338,377	15.32%
Woodford Investment Management LLP	19.08.2014	–	21,703,125	–	21,703,125	5.36%
Investec Asset Management Limited	19.12.2016	–	20,204,001	–	20,204,001	4.97%
Artemis Investment Management LLP	06.05.2016	–	20,278,415	–	20,278,415	4.99%
Orbis Holdings Limited	01.12.2016	–	20,241,875	–	20,241,875	4.98%

Notes:
Ordinary shares of $11^{16}/_{29}$ pence each
(1) As at 31 December 2016, Invesco plc had voting rights over 93,521,993 shares. All other shareholdings were as stated in this table as at 31 December 2016.
(2) As at the date of the last notification made to the Company by the investor, in compliance with DTR.

Authority to purchase own shares

At the AGM held on 20 April 2016, shareholders authorised the Company to make market purchases of up to 10% of the issued ordinary share capital. At the forthcoming AGM, shareholders will be asked to renew this authority.

The Company did not purchase any of its own shares during 2016, nor has it done so from 31 December 2016 up to the date of this report.

Rights and obligations attaching to shares

There are various rights and obligations attaching to the ordinary shares which are set out in the Articles. A copy of the Articles can be accessed on the Company's website at http://www.drax.com/about-us/compliance-and-policies/

Attention should be given to the following sections within the Articles, covering the rights and obligations attaching to shares:

Variation of rights – which covers the rights attached to any class of shares that may be varied with the written consent of the holders of not less than three-quarters in nominal value of the issued shares of that class, or with the sanction of an extraordinary resolution passed at a separate General Meeting of the holders of those shares.

Transfer of shares – provides detail of how transfers of shares in certified and uncertified form may be undertaken. It also sets out the directors' rights of refusal to effect a transfer and the action that directors must take following such refusal. It should be noted that a shareholder does not need to obtain the approval of the Company, or of other holders of shares in the Company, for a transfer of shares to take place.

Voting and deadlines for exercising voting rights – these sections of the Articles deal with voting on a show of hands and on a poll. They also cover the appointment of a proxy or corporate representative. In respect of voting deadlines, the Articles provide for the submission of proxy forms not less than 48 hours before the time appointed for the holding of the meeting. It has been the Company's practice since incorporation to hold a poll on every resolution at Annual General Meetings and Extraordinary General Meetings.

A trustee holds shares on behalf of employees in respect of the Group's Share Incentive Plan. The voting rights attached to such shares are not directly exercisable by the employees. The employee may direct the trustee on how to vote at a General Meeting and the trustee may only cast its vote in respect of shares over which it has received a valid direction from employees.

Changes to the Articles – the Articles may only be changed by shareholders by special resolution.

Other significant agreements

In the Group's financing agreements, as detailed below, on a change of control, if any lender requires, it may by giving notice to the relevant Group entity within 30 days of receiving notice from such Group entity that a change of control has occurred, cancel its commitments and require the repayment of its share of any outstanding amounts within three business days of such cancellation notice being given.

The financing agreements comprise:

- The £100 million amortising term loan facility agreement dated 20 December 2012 (as amended and restated on 8 December 2015) between, amongst others, Drax Finance Limited and the Prudential M&G UK Companies Financing Fund.
- The £50 million amortising term loan facility agreement dated 20 December 2012 (as amended and restated on 8 December 2015) between, amongst others, Drax Finance Limited and the Green Investment Bank.
- The £400 million revolving credit facility agreement dated 20 December 2012 (as amended and restated on 8 December 2015) between, amongst others, Drax Power Limited and Barclays Bank PLC (as facility agent).
- The £75 million guarantee and reimbursement arrangement issued by The Lords Commissioners of Her Majesty's Treasury dated 23 April 2013 (as amended and restated on 8 December 2015) in respect of a £75 million guaranteed loan note instrument issued by Drax Finance Limited to Friends Life Limited.
- Two note purchase agreements dated 8 May 2014 (as amended and restated on 8 December 2015) of £100 million in aggregate, in each case between Drax Finance Limited and various funds managed by M&G Investments.

Under the terms of the above financing agreements, a "change of control" occurs if any person or group of persons acting in concert gains control of Drax Group plc.

In addition to the above, on 6 December 2016, Drax Group plc entered into a commitment for a £375 million acquisition facility. Once the subsequent financing agreement is signed, a "change of control" occurs if any person or group of persons acting in concert gains control of Drax Group plc or Drax Group Holdings Limited.

There are no other significant agreements to which the Group is a party that take effect, alter or terminate upon a change of control of the Group following a takeover bid.

Strategic report

The Strategic report on pages 1 to 61 contains disclosures in relation to employee participation, Greenhouse Gas emissions and third party indemnity provisions for which the Company is responsible.

Disabled employees

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned.

In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues, and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, so far as possible, be identical to that of other employees.

Auditors and the disclosure of information to the auditor

So far as each person serving as a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing the report, of which the auditor is unaware. Having made enquiries of fellow directors, each director has taken all steps that he/she ought to have taken as a director to ascertain any relevant audit information and to establish that the auditor is aware of that information. This information is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act.

Resolutions will be proposed at the AGM for (i) the reappointment of Deloitte LLP as the auditor of the Group; and (ii) authorising the directors to determine the auditor's remuneration. As explained, the Audit Committee reviews the appointment of the auditor, the auditor's effectiveness and its relationship with the Group, including the level of audit and non-audit fees paid to the auditor. Further details on the work of the auditor and the Audit Committee are set out in the Audit Committee report on pages 77 to 81.

The directors' report was approved by the Board on 15 February 2017 and is signed on its behalf by:

David McCallum
Group Company Secretary

Registered office:
Drax Power Station
Selby
North Yorkshire
YO8 8PH
Registered in England and Wales No. 5562053

DIRECTOR'S RESPONSIBILITIES STATEMENT

The directors are responsible for preparing the Annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), set out in FRS 101 "Reduced Disclosure Framework". Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing the Parent Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In preparing the Group financial statements, International Accounting Standard 1 requires that directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

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

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the Strategic report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

This responsibility statement was approved by the Board of directors on 15 February 2017 and is signed on its behalf by:

Dorothy Thompson CBE
Chief Executive, Drax Group

Will Gardiner
Chief Financial Officer

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DRAX GROUP PLC

Opinion on financial statements of Drax Group plc
In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2016 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including FRS 101 "Reduced Disclosure Framework; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

The financial statements that we have audited comprise:

- the Consolidated Income Statement;
- the Consolidated Statement of Comprehensive Income;
- the Consolidated and Parent Company Balance Sheets;
- the Consolidated Cash Flow Statement;
- the Consolidated and Parent Company Statement of Changes in Equity;
- the related Group notes 2.1 to 8.4 and
- the related Parent Company notes 1 to 8.

The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

Summary of our audit approach

Key risks	The key risks that we identified in the current year were: – Asset impairment – Useful economic life assumptions – Valuation of commodity and foreign exchange contracts – Existence and valuation of biomass stocks – Valuation and recoverability of ROCs
Materiality	The materiality that we used in the current year was £4.2 million which was determined based on a blended basis taking into consideration a number of available metrics.
Scoping	We focused our group audit scope primarily on the audit work at three locations, being Drax Power, Haven Power and Drax Biomass. All of these were subject to a full scope audit. These three locations represent the principal business units and account for all of the group's net assets, revenue and profit before tax.
Significant changes in our approach	Our audit approach remains consistent to the prior year. We have refined our key risk in relation to stocks and have focused specifically on biomass existence and valuation and identified a new risk in relation to the useful economic life assumptions adopted.

Going concern and the directors' assessment of the principal risks that would threaten the solvency or liquidity of the group

We are required to state whether we have anything material to add or draw attention to in relation to: – the directors' confirmation on page 61 that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity; – the disclosures on pages 55 to 61 that describe those risks and explain how they are being managed or mitigated; – the directors' statement on page 111 about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the group's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements; and – the directors' explanation on page 54 as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	We confirm that we have nothing material to add or draw attention to in respect of these matters. We agreed with the directors' adoption of the going concern basis of accounting and we did not identify any such material uncertainties. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's ability to continue as a going concern.

Independence

We are required to comply with the Financial Reporting Council's Ethical Standards for Auditors and confirm that we are independent of the group and we have fulfilled our other ethical responsibilities in accordance with those standards.	We confirm that we are independent of the group and we have fulfilled our other ethical responsibilities in accordance with those standards. We also confirm we have not provided any of the prohibited non-audit services referred to in those standards.

Our assessment of risks of material misstatement

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team.

This year we have refined the risk relating to stocks to focus on the existence and valuation of biomass stocks, as opposed to coal and biomass stocks in the prior year as this is where we consider the most judgement to exist. As per note 3.3, biomass stocks have increased from £119 million at 31 December 2015 to £198 million at 31 December 2016. Coal stocks have reduced from £89 million at 31 December 2015 to £66 million at 31 December 2016. This reflects the development of the plant.

Useful economic life assumptions has been identified as a new risk in the year. As part of the most recent annual review of asset lives, the estimated useful life of coal-specific assets at Drax Power Station will be revised with effect from 1 January 2017 and this is considered to be a key judgement.

Risk	How the scope of our audit responded to the risk
Asset Impairment The Group's market capitalisation continues to be below its asset value. Additional contributing factors in the current year which increase the risk of impairment includes the depreciation of sterling following the Brexit vote, delays in the approval of the CfD, the UK Government consultation on the future of coal generating assets within the UK power industry and continued softness in commodity markets. Management has therefore performed an impairment review in the current year. As noted in the Group's critical accounting judgements, estimates and assumptions in note 2.4 and the Audit Committee report on page 77, asset impairment has been considered a key risk by the Audit Committee. The impairment testing is subject to the application of management judgement in identifying cash-generating units (CGUs) and various assumptions underlying the calculation of the value in use for each CGU identified. This assessment also considers changes in the business which may give rise to additional CGUs, for example the approval of the CfD on Unit 1 in the current year. Additionally, these assumptions include the achievability of the long-term business plan and related modelling assumptions underlying the valuation process. The significant judgements have been disclosed by management in note 2.4 and include: – The expected operating lives of the six generating units – Future commodity prices beyond the horizon of existing contracted purchases, particularly long-term power prices at both baseload and peak times, and biomass prices in the long term given that biomass is not a standardised commodity traded openly on exchanges; – Future foreign exchange rates beyond the horizon of existing contracted purchase commitments; – the continuance of existing biomass support regimes until 2027 and the existence of a favourable economic environment for biomass generation thereafter; and – The discount rate applied to forecast future cash flows.	We carried out testing of the design and implementation of key controls related to asset impairment. We have challenged management's identification of CGUs, taking into consideration the independence of cash flows across key components of the business and generating units. We utilised our valuation specialists to benchmark key market related assumptions including commodity prices, current and future capacity and other support mechanisms and discount rates against external data where available. For example, we have compared the commodity price assumptions to the latest available Department for Business, Energy and Industrial Strategy (DBEIS), Department of Energy and Climate Change (DECC) and National Grid forecasts. We have considered the liquidity of the biomass market and the impact that Drax could have on that market relating to the volumes of biomass required in the future. We have also challenged the underlying assumptions and significant judgements used in management's impairment model by: – Running a range of sensitivities to assess whether an impairment would be required if a range of more conservative assumptions were adopted; – Assessing the historical accuracy of management's budgets and forecasts by comparing them to actual performance and verifying the mathematical accuracy of the cash flow models; and – Assessing whether the disclosures in note 2.4 of the financial statements appropriately disclose the key judgements taken so that the reader of the accounts is aware of the impact of the financial statement of changes to key assumptions that may lead to impairment.
Useful economic life assumptions Previously, the useful economic life of the power station was assumed to end in 2039. Estimated useful lives are based on past experience, future replacement cycles and other available evidence; however an inherent degree of judgement remains. As per note 3.1, as part of the most recent annual review of asset lives, the estimated useful life of coal-specific assets at Drax Power Station will be revised with effect from 1 January 2017. On 9 November 2016 the Government announced a consultation on the future closure of unabated coal-fired generation. Following this, management concluded that coal generation will most likely cease during 2025, shortening the useful lives of the coal-specific assets which will not be required to support generation after this date. Management believe this change will result in an increase of approximately £27 million per annum in depreciation charges from 1 January 2017 to 31 December 2025.	We have considered a number of factors as part of our audit including challenging the reasonableness of key assumptions such as: – the adequacy of the current and proposed depreciation assumptions across the generation asset base; – consideration of the future ability to generate economic value; – factors affecting primary income streams including forecast spreads and external factors including political and regulatory requirements; and – Consistency of the UEL assessment with the impairment analysis above. We have also assessed whether 1 January 2017 is an appropriate date from which to amend the useful economic life.

Risk	How the scope of our audit responded to the risk
Valuation of commodity and foreign exchange contracts Unrealised gains on derivative contracts recognised in the income statement are £177m (2015: £124m), with total assets of £891m and liabilities of £364m recognised on the balance sheet as at the year end. We note that £666m of assets relate to foreign currency derivatives at the current year end (2015: £36m). The valuation of derivative contracts is complex and requires judgement in areas including the selection of appropriate valuation methodologies and assumptions in respect of future market prices and credit risk factors. Further detail of the key judgements are disclosure in the Group's critical accounting judgements, estimates and assumptions set out on pages 117 and 118 and the Audit Committee report on page 77.	We carried out testing of the design and implementation of key controls related to the valuation of commodity and foreign exchange contracts. We used our financial instrument specialists to test management's key judgements and calculations, including testing a sample of trades undertaken to trade tickets confirming key information such as volumes and contracted prices. We have assessed the valuation models used by management to determine the fair value of the derivative instruments and performed independent valuations across a sample of both commodity and foreign exchange contracts. We have analysed the appropriateness of management's forward price curve assumptions by benchmarking these to third party sources and reviewed the consistency of the assumptions used across other areas of the financial statements such as asset impairment. We have challenged management's approach and assumptions involved in assessing fair value adjustment such as credit risk, time value of money and spread adjustments.
Existence and valuation of biomass stocks Biomass stocks of £198 million (2015: £119 million) are held on the balance sheet at year end. The most significant judgement relating to stock is considered to be the existence and valuation of biomass stocks held on-site £21 million. Given the storage and handling characteristics of the on-site biomass stocks, judgement is inherent in calculating the volume of biomass stocks owned by the Group because it is not practical to physically count the stocks at year end. Further details of the key accounting policy judgements are included in note 3.3, and as noted, the calibrated weighers and efficiency calculations are subject to a range of tolerable errors. The valuation of biomass is dependent upon the estimation or measurement of the tonnage held, the calorific value, its purchase price and its net realisable value. The weighted average cost calculation is complex and dependant on the tonnage held. This results in an increasing risk of management error or bias and therefore increased risk of misstatement.	We carried out testing of the design and implementation of key controls related to the existence and valuation of on-site biomass stocks. Our audit procedures include testing the underlying weighted average cost calculation by agreeing key inputs such as price and volumes to source data including purchase invoices for amounts delivered in the year. We also sample testing the calorific value of biomass to third party laboratory reports or purchase invoice as appropriate. We gained assurance of stock volumes on site during the year through management's dome emptying programme. We also sample tested metering data subsequent to the dome emptying by agreeing to third party sources and internal operational data. We assessed the tolerable errors in the weighing equipment through agreement to a sample of third party calibration certificates.
Valuation and recoverability of ROCs ROCs with a value of £258 million are held on the balance sheet at the year end (2015: £266 million). ROCs are recognised as they are earned through generating electricity from burning biomass. They are initially recognised at fair value (reducing the cost of biomass consumed in the income statement) and subsequently written down to net realisable values as appropriate. Judgement is required by management in estimating both the initial fair value and estimating net realisable value, including value recovered through the recycling fund. Further detail is explained in the Group's critical accounting judgements, estimates and assumptions set out on pages 117 and 118 and in the Audit Committee report on page 77.	We carried out testing of the design and implementation of key controls related to the valuation of ROCs. We gained assurance over the ROCs generated in the year by agreement to Ofgem confirmation certificates and operational data confirming the level of generation eligible for ROCs. We have assessed the initial fair value of ROCs by agreement of the buy-out price to available third party supporting information and external sales agreements. We have also challenged the estimates made by management of the recoveries through the recycling fund, the level of which impacts the estimated net realisable value of the ROCs held in the balance sheet at year end. This included comparison to other available third party estimates.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

When determining materiality, we considered the decline in earnings this year and at present do not consider that this decline is likely to reflect a long-term reduction in the size and scale of the business.

We have determined materiality by considering a range of possible benchmarks and the figures derived from those, with a particular focus on selecting a materiality within the range that we considered appropriate. This included underlying EBITDA (excluding unrealised gains or losses on derivative contracts, one-off asset obsolescence charges and losses on disposal of assets), profit before and after interest and tax as well as the scale of the balance sheet and the overall size of the business. We determined materiality for the Group on a blended basis to be £4.2 million (2015: £6.1 million).

This materiality equates to 0.2% of net assets and 17% of underlying profit before tax (excluding unrealised gains or losses on derivative contracts, one-off asset obsolesce charges and losses on disposal of assets). Last year materiality was also based on a blended rate.

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.2 million (2015: £0.1 million), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. The change in the reporting threshold has been made following our reassessment of what matters require communicating. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

An overview of the scope of our audit

Our group audit was scoped by obtaining an understanding of the group and its environment, including group-wide controls, and assessing the risks of material misstatement at the group level. Based on that assessment, we focused our group audit scope primarily on the audit work at three locations (2015: the same three locations), being Drax Power, Haven Power and Drax Biomass. All of these locations were subject to a full scope audit and they represent the principal business units and account for all of the group's net assets, revenue and profit before tax, in line with 2015. There were also selected to provide an appropriate basis for undertaking audit work to address the risks of material misstatement identified above. Our audit work at three locations was executed at levels of materiality applicable to each individual entity which were lower than group materiality and ranged from £2.1 million to £3.8 million (2015: £3.0 million to £4.8 million).

At the parent entity level we also tested the consolidation process and carried out analytical procedures to confirm our conclusion that there were no significant risks of material misstatement of the aggregated financial information of the remaining components not subject to audit or audit of specified account balances.

The group audit team continued to follow a programme of planned visits that has been designed so that the Senior Statutory Auditor visits each of the locations where the group audit scope was focused at least once every two years and the most significant of them at least once a year. During 2016 the Senior Statutory Auditor visited two of these locations, and other senior team members visited the third.

Opinion on other matters prescribed by the Companies Act 2006

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

– the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
– the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
– the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report and the Directors' Report.

Matters on which we are required to report by exception

Adequacy of explanations received and accounting records Under the Companies Act 2006 we are required to report to you if, in our opinion: – we have not received all the information and explanations we require for our audit; or – adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or – the parent company financial statements are not in agreement with the accounting records and returns.	We have nothing to report in respect of these matters.
Directors' remuneration Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made or the part of the Directors' Remuneration Report to be audited is not in agreement with the accounting records and returns.	We have nothing to report arising from these matters.
Corporate Governance Statement Under the Listing Rules we are also required to review part of the Corporate Governance Statement relating to the company's compliance with certain provisions of the UK Corporate Governance Code.	We have nothing to report arising from our review.
Our duty to read other information in the Annual report Under International Standards on Auditing (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is: – materially inconsistent with the information in the audited financial statements; or – apparently materially incorrect based on, or materially inconsistent with, our knowledge of the group acquired in the course of performing our audit; or – otherwise misleading. In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed.	We confirm that we have not identified any such inconsistencies or misleading statements.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). We also comply with International Standard on Quality Control 1 (UK and Ireland). Our audit methodology and tools aim to ensure that our quality control procedures are effective, understood and applied. Our quality controls and systems include our dedicated professional standards review team and independent partner reviews.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Scope of the audit of the financial statements

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

James Leigh, FCA (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, UK
15 February 2017

FINANCIAL STATEMENTS

Introduction

The consolidated financial statements provide detailed information about the financial performance (Consolidated income statement), financial position (Consolidated balance sheet), and cash flows (Consolidated cash flow statement) of Drax Group plc (the Company) together with all of the entities controlled by the Company (collectively, the Group).

The notes to the financial statements provide additional information on the items in the Consolidated income statement, Consolidated balance sheet and Consolidated cash flow statement. The notes include explanations of the information presented. In general, the additional information in the notes to the financial statements is required by law, International Financial Reporting Standards (IFRS) or other regulations to facilitate increased understanding of the primary statements set out on pages 120 to 124.

Basis of preparation

The financial statements have been prepared in accordance with IFRS as adopted by the European Union and therefore the consolidated financial statements comply with Article 4 of the EU IAS Regulation.

The financial statements have been prepared on the historical cost basis, except for certain financial assets and liabilities that have been measured at fair value.

Going concern

The Group's business activities, along with future developments that may affect its financial performance, position and cash flows, are set out within the Strategic report on pages 1 to 61 of this document.

In the viability statement on page 54 the directors state that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the next three years.

Consequently, the directors also have a reasonable expectation that the Group will continue in existence for the next 12 months and, therefore, have adopted the going concern basis in preparing these financial statements.

Changes in foreign currency exchange rates

The substantial depreciation of Sterling against the US dollar and Euro during the second half of 2016 has had a material impact on our financial statements, resulting in a significant increase in the fair value of our forward currency purchase contracts in the balance sheet and income statement volatility due to realised and unrealised currency exchange gains and losses.

Where the impact is material, we have extended certain disclosures to highlight the impact of currency exchange gains and losses in the period. Where relevant, we have re-presented the prior year comparatives to provide the relevant information to gauge the impact.

Basis of consolidation

These consolidated financial statements incorporate the financial results of the Company and of all entities controlled by the Company, (its subsidiaries) made up to 31 December each year. The Company owns 100% of the equity of all subsidiaries.

The impact of all intra-Group transactions are eliminated on consolidation. The results of subsidiaries acquired or disposed of during the year are included in the Consolidated income statement from the date the Company gains control until the date when the Company ceases to control the subsidiary.

Accounting policies

Those accounting policies that are material to our financial statements are described in note 8.3 to the financial statements or, where specific to an individual component of the financial statements, in the relevant note (see contents on page 119).

We have not changed any of our accounting policies in the period; however we have adopted a material new policy in respect of accounting for the Contract for Difference (CfD) (see page 118).

A full listing of new standards, interpretations and pronouncements under IFRS applicable to these financial statements is presented in note 8.2. The application of these new requirements has not had a material effect on the financial statements.

Judgements, estimates and uncertainties

The preparation of financial statements requires management to exercise judgement in applying the Group's accounting policies. 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 revised 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, estimates and assumptions

The judgements that carry the most significant risk of an outcome that differs from the amount recognised in the financial statements are as follows:

Property, plant and equipment – property, plant and equipment is depreciated on a straight-line basis over its useful economic life. Estimated useful lives are based on past experience, future replacement cycles and other available evidence. However, a degree of judgement is required. Useful economic lives are reviewed annually, we reduced the useful lives of certain assets in our generation business from 1 January 2017.

MORE INFORMATION: note 3.1 on page 137

Impairment – an impairment review is conducted annually for goodwill and for other assets and cash-generating units where an indicator of possible impairment exists. The assessment of future cash flows that underpins such a review is based on management's best estimate of future prices, volumes and economic conditions. The calculations are particularly sensitive to judgement given the long time period covered by the assessment.

MORE INFORMATION: note 2.4 on page 130

Derivatives – derivative financial instruments are recorded in the Group's balance sheet at fair value. The assessment of fair value is derived from assuming a market price for the instrument in question. The Group bases its assessment of market prices upon forward curves that are largely derived from readily obtainable quotations and third party sources. However, any forward curve is based at least in part upon assumptions about future transactions and market movements. Where such instruments extend beyond the liquid portion of the forward curve, the level of judgement increases as the number of observable transactions decreases.

MORE INFORMATION: note 7.2 on page 160

Inventories – fuel inventories are valued at weighted average cost based on purchase price, or net realisable value where lower. Valuation is largely based on observable data (such as invoiced costs and automated weigher readings). However, given the bulk nature of fuels an element of judgement is required to assess the volume of stock held at the balance sheet date.

MORE INFORMATION: note 3.3 on page 140

Renewable Obligation Certificates (ROCs) – the carrying amount of ROCs in the Group's balance sheet is stated at their expected realisable value. This assessment is based on estimated future sales prices, which involves judgement.

MORE INFORMATION: note 3.2 on page 139

Other accounting judgements, estimates and assumptions

Pensions – the Group records a liability in its balance sheet for its obligation to provide benefits under an approved defined benefit pension scheme less the fair value of assets held by the pension scheme. The actuarial valuation of the scheme assets and liabilities is performed annually and depends on assumptions regarding interest rates, inflation, future salary and pension increases, mortality and other factors.

MORE INFORMATION: note 6.3 on page 152

Taxation – in accounting for tax liabilities the Group makes assumptions 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 advisors.

MORE INFORMATION: note 2.6 on page 132

Revenue recognition – the nature of some of the Group's activities, particularly within the Retail segment, results in revenue being based on the estimated volumes of power supplied to customers at an estimated average price per unit. Assumptions that underpin these estimates are applied consistently and comparison of past estimates to final settlements suggests a high degree of accuracy. However, given the level of judgement involved, actual outcomes may vary from initial estimates.

MORE INFORMATION: note 2.2 on page 127

CfD accounting policy – the CfD is a material new contract for the Group and the specific accounting treatment is not prescribed by an existing IFRS. Accordingly, management has had to exercise judgement in adopting an appropriate policy in accordance with IAS 8. Management considered the requirements of a number of standards, including IAS 18 (revenue), IAS 39 (financial instruments), IAS 16 (leases) and IAS 20 (Government Grants) in determining the policy to be adopted. In particular, management concluded that the contract did not meet the definition of a derivative financial instrument in IAS 39 on the grounds that cash flows do not become contractually due until the point of generation and the Group is under no obligation to generate. Accordingly, amounts due under the CfD are recognised at the point of generation.

MORE INFORMATION: note 2.2 on page 127

Non-IFRS measures of financial performance

We present two non-IFRS measures on the face of our income statement: EBITDA and underlying profit.

EBITDA is the primary measure we use to assess our financial performance. EBITDA is defined as profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.

Underlying measures, including underlying profit before and after tax and underlying earnings per share (EPS), exclude the impact of unrealised gains and losses on derivative contracts, plus particular transactions considered to be one-off in nature that do not reflect the underlying trading and operational performance of the Group. Underlying profit after tax and EPS exclude the post-tax effect of these items. In 2015, this excluded an asset obsolescence charge of £109 million. In 2016, this excludes a deferred tax credit of £31 million in relation to start-up losses in our US business.

A reconciliation of profit for the year attributable to equity holders (calculated in accordance with IFRS) to underlying profit after tax is provided in note 2.7.

Under our current distribution policy, dividends are calculated based upon 50% of underlying profit after tax.

CONTENTS

SECTION 1:

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT

	Notes	Years ended 31 December 2016 £m	2015 £m
Revenue	2.2	**2,949.8**	3,065.0
Fuel costs in respect of generation		**(1,154.2)**	(1,309.9)
Cost of power purchases		**(907.8)**	(851.3)
Grid charges		**(379.7)**	(369.5)
Other retail costs		**(131.8)**	(125.5)
Total cost of sales		**(2,573.5)**	(2,656.2)
Gross profit		**376.3**	408.8
Operating and administrative expenses	2.3	**(236.3)**	(239.8)
EBITDA[1]	2.3	**140.0**	169.0
Depreciation	3.1	**(109.5)**	(100.4)
Asset obsolescence charges		**–**	(109.2)
Loss on disposal		**(3.8)**	(7.1)
Unrealised gains on derivative contracts	7.2	**176.8**	123.7
Operating profit		**203.5**	76.0
Interest payable and similar charges	2.5	**(7.0)**	(18.4)
Interest receivable	2.5	**0.6**	1.4
Profit before tax		**197.1**	59.0
Tax:			
– Before effect of changes in rate of corporation tax	2.6	**(13.0)**	(20.5)
– Effect of changes in rate of corporation tax	2.6	**9.8**	17.8
Total tax charge		**(3.2)**	(2.7)
Profit for the year attributable to equity holders		**193.9**	56.3
Underlying profit after tax[2]	2.7	**20.5**	46.0
Earnings per share		**pence**	pence
– Basic	2.7	**48**	14
– Diluted		**47**	14

All results relate to continuing operations.

Notes:

(1) EBITDA is profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.

(2) Underlying profit after tax excludes the post-tax effect of unrealised gains and losses on derivative contracts, plus particular transactions considered to be one-off in nature that do not reflect the underlying trading performance of the Group. A reconciliation of profit after tax (calculated in accordance with IFRS) to underlying profit after tax is provided in note 2.7.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Notes	Years ended 31 December 2016 £m	2015 £m
Profit for the year		**193.9**	56.3
Items that will not be reclassified subsequently to profit or loss:			
Actuarial (losses)/gains on defined benefit pension scheme	6.3	**(8.4)**	1.2
Deferred tax on actuarial (losses)/gains on defined benefit pension scheme	2.6	**1.6**	(0.2)
Items that may be subsequently reclassified to profit or loss:			
Exchange differences on translation of foreign operations		**(9.1)**	(2.9)
Fair value gains on cash flow hedges	7.2	**330.1**	23.4
Deferred tax on cash flow hedges before corporation tax rate change	2.6	**(62.6)**	(4.7)
Impact of corporation tax rate change on deferred tax on cash flow hedges	2.6	**3.0**	(0.2)
Other comprehensive income		**254.6**	16.6
Total comprehensive income for the year attributable to equity holders		**448.5**	72.9

CONSOLIDATED BALANCE SHEET

	Notes	As at 31 December 2016 £m	2015 £m
Assets			
Non-current assets			
Goodwill and other intangible assets	5.2	**36.2**	26.3
Property, plant and equipment	3.1	**1,641.5**	1,653.8
Deferred tax assets	2.6	**33.5**	–
Derivative financial instruments	7.2	**486.3**	278.4
		2,197.5	1,958.5
Current assets			
Inventories	3.3	**287.5**	224.0
ROC and LEC assets	3.2	**257.6**	270.1
Trade and other receivables	3.4	**292.9**	319.3
Derivative financial instruments	7.2	**405.0**	330.8
Cash and cash equivalents	4.2	**228.4**	133.8
Current tax assets		**–**	0.6
		1,471.4	1,278.6
Liabilities			
Current liabilities			
Trade and other payables	3.5	**591.9**	488.0
Current tax liabilities		**6.1**	–
Borrowings	4.3	**35.9**	0.3
Derivative financial instruments	7.2	**251.0**	274.3
		884.9	762.6
Net current assets		**586.5**	516.0
Non-current liabilities			
Borrowings	4.3	**286.0**	320.1
Derivative financial instruments	7.2	**112.5**	300.1
Provisions	5.3	**35.0**	30.5
Deferred tax liabilities	2.6	**275.2**	191.9
Retirement benefit obligations	6.3	**30.1**	29.5
		738.8	872.1
Net assets		**2,045.2**	1,602.4
Shareholders' equity			
Issued equity	4.5	**47.0**	46.9
Capital redemption reserve	4.5	**1.5**	1.5
Share premium	4.5	**424.2**	424.2
Merger reserve	4.5	**710.8**	710.8
Hedge reserve	7.4	**305.4**	34.9
Translation reserve	4.5	**(10.2)**	(1.1)
Retained profits	2.9	**566.5**	385.2
Total shareholders' equity		**2,045.2**	1,602.4

The consolidated financial statements of Drax Group plc, registered number 5562053, were approved and authorised for issue by the Board of directors on 15 February 2017.

Signed on behalf of the Board of directors:

Dorothy Thompson CBE
Chief Executive

Will Gardiner
Chief Financial Officer

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Issued equity £m	Capital redemption reserve £m	Share premium £m	Merger reserve £m	Hedge reserve £m	Translation reserve £m	Retained profits £m	Total £m
At 1 January 2015	46.8	1.5	422.8	710.8	16.4	1.8	372.5	1,572.6
Profit for the year	–	–	–	–	–	–	56.3	56.3
Other comprehensive income/(expense)	–	–	–	–	18.5	(2.9)	1.0	16.6
Total comprehensive income for the year	–	–	–	–	18.5	(2.9)	57.3	72.9
Equity dividends paid (note 2.8)	–	–	–	–	–	–	(49.9)	(49.9)
Issue of share capital (note 4.5)	0.1	–	1.4	–	–	–	–	1.5
Movement in equity associated with share-based payments (note 6.2)	–	–	–	–	–	–	5.3	5.3
At 1 January 2016	**46.9**	**1.5**	**424.2**	**710.8**	**34.9**	**(1.1)**	**385.2**	**1,602.4**
Profit for the year	–	–	–	–	–	–	193.9	193.9
Other comprehensive income/(expense)	–	–	–	–	270.5	(9.1)	(6.8)	254.6
Total comprehensive income for the year	–	–	–	–	270.5	(9.1)	187.1	448.5
Equity dividends paid (note 2.8)	–	–	–	–	–	–	(11.0)	(11.0)
Issue of share capital (note 4.5)	0.1	–	–	–	–	–	–	0.1
Movement in equity associated with share-based payments (note 6.2)	–	–	–	–	–	–	5.2	5.2
At 31 December 2016	**47.0**	**1.5**	**424.2**	**710.8**	**305.4**	**(10.2)**	**566.5**	**2,045.2**

CONSOLIDATED CASH FLOW STATEMENT

	Notes	Years ended 31 December 2016 £m	2015 £m
Cash generated from operations	4.4	**213.1**	166.0
Income taxes paid		**(1.7)**	(3.8)
Other gains/(losses)		**0.7**	(3.7)
Interest paid		**(21.7)**	(11.9)
Interest received		**0.4**	1.5
Net cash from operating activities		**190.8**	148.1
Cash flows from investing activities			
Purchases of property, plant and equipment		**(93.2)**	(179.1)
Acquisition of subsidiary		**–**	(4.0)
Redemption of short-term investments		**–**	40.1
Net cash used in investing activities		**(93.2)**	(143.0)
Cash flows from financing activities			
Equity dividends paid	2.8	**(11.0)**	(49.9)
Proceeds from issue of share capital		**0.1**	1.5
Repayment of borrowings		**–**	–
Other financing costs paid		**–**	(5.7)
Net cash absorbed by financing activities		**(10.9)**	(54.1)
Net increase/(decrease) in cash and cash equivalents		**86.7**	(49.0)
Cash and cash equivalents at 1 January		**133.8**	180.9
Effect of changes in foreign exchange rates		**7.9**	1.9
Cash and cash equivalents at 31 December	4.2	**228.4**	133.8

SECTION 2:

FINANCIAL PERFORMANCE

The financial performance section gives further detail on the information in the Consolidated income statement. It includes a summary of financial performance by business unit (2.1), analysis of certain income statement items (2.2–2.6) and information regarding underlying earnings, distributable profits and dividends (2.7–2.9). Further commentary regarding our trading and operational performance during the year, which is predominantly reflected in EBITDA, can be found in the Strategic report on pages 1 to 61, with particular reference to key achievements and market conditions that have affected our results.

2.1 Segmental reporting

The Group is organised into three businesses, with a dedicated management team for each, and a central head office providing certain corporate functions. Our businesses are:

- Generation: the generation of electricity at Drax Power Station;
- Biomass Supply: production of sustainable compressed wood pellets at our processing facilities in the US; and
- Retail: the supply of power to business customers and wood pellets to the domestic heat market.

Each business is an operating segment for the purpose of segmental reporting. Information reported to the Board for the purposes of assessing performance and making investment decisions is based on these three operating segments. The measure of profit or loss for each reportable segment presented to the Board on a regular basis is EBITDA (as defined on page 118).

Operating costs are allocated to segments to the extent they are directly attributable to the activities of that segment. Head office costs are included within central operating costs.

Segment revenues and results

The following is an analysis of the Group's revenues and results by reporting segment for the year ended 31 December 2016:

	Year ended 31 December 2016				
	Generation £m	Retail £m	Biomass Supply £m	Adjustments[1] £m	Consolidated £m
Revenue					
External sales	1,622.7	1,326.4	0.7	–	2,949.8
Inter-segment sales	868.2	–	72.9	(941.1)	–
Total revenue	2,490.9	1,326.4	73.6	(941.1)	2,949.8
Segment gross profit	337.0	23.5	18.1	(2.3)	376.3
Segment EBITDA	173.8	(4.3)	(6.3)	(2.3)	160.9
Central costs					(20.9)
Consolidated EBITDA					140.0
Depreciation and amortisation					(109.5)
Losses on disposal					(3.8)
Unrealised gains on derivative contracts					176.8
Operating profit					203.5
Net finance costs					(6.4)
Profit before tax					197.1

Notes:
(1) Adjustments represent the elimination of intra-group transactions.

2.1 Segmental reporting continued

The following is an analysis of the Group's revenues and results by reporting segment for the year ended 31 December 2015:

	Year ended 31 December 2015				
	Generation £m	Retail £m	Biomass Supply £m	Adjustments[1] £m	Consolidated £m
Revenue					
External sales	1,775.0	1,290.0	–	–	3,065.0
Inter-segment sales	863.2	–	28.4	(891.6)	–
Total revenue	2,638.2	1,290.0	28.4	(891.6)	3,065.0
Segment gross profit	390.1	19.3	1.0	(1.6)	408.8
Segment EBITDA	214.6	(6.3)	(14.8)		193.5
Central costs					(24.5)
Consolidated EBITDA					169.0
Depreciation and amortisation					(100.4)
Losses on disposal					(7.1)
Asset obsolescence charges[2]					(109.2)
Unrealised gains on derivative contracts					123.7
Operating profit					76.0
Net finance costs					(17.0)
Profit before tax					59.0

Notes:
(1) Adjustments represent the elimination of intra-group transactions.
(2) £102.6 million of the asset obsolescence charges arose in the Generation segment, with the remaining £6.6 in the Biomass Supply segment.

Assets and working capital are monitored on a consolidated basis, with no separate reporting by segment in the Group's management accounts. However, spend on key capital projects is monitored. Total spend on the biomass transformation project during 2016 was £29 million (2015: £90 million), of which £7 million (2015: £22 million) relates to construction of assets, in the US, within the Biomass Supply segment.

The accounting policies applied for the purpose of measuring the segments' profits or losses, assets and liabilities are the same as those used in measuring the corresponding amounts in the Group's financial statements. The external revenues and results of all of our reporting segments are subject to seasonality with higher despatch and prices in the winter months, compared to summer months.

Intra-group trading

Intra-group transactions are carried out on arm's-length, commercial terms that where possible equate to market prices at the time of the transaction. During 2016, the Biomass Supply segment sold wood pellets with a total value of £72.9 million (2015: £28.4 million) to the Generation segment and the Generation segment sold power, ROCs and LECs with a total value of £868.2 million (2015: £863.2 million) to the Retail segment.

The impact of all intra-group transactions, including any unrealised profit arising (£2.3 million at 31 December 2016), is eliminated on consolidation.

Major customers

Total revenue for the year ended 31 December 2016 includes amounts of £541.5 million and £399.3 million (2015: £597.7 million and £468.0 million) derived from two customers (2015: two customers), each representing 10% or more of the Group's consolidated revenue for the year. These revenues arose in the Generation segment.

2.2 Revenue

Accounting Policy

Revenue represents amounts 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 with or between Group companies.

Revenues from the sale of electricity from our generating assets in Drax Power are measured based upon metered output delivered at rates specified under contract terms or prevailing market rates as applicable.

Two of our biomass-fuelled generating units earn Renewable Obligation Certificates (ROCs) under the UK Government's Renewables Obligation (RO) regime. The financial benefit of a ROC is recognised in the income statement at the point the relevant renewable biomass fuel is burnt and power dispatched as a reduction in the cost of the biomass fuel. A corresponding asset is recognised on the balance sheet (see note 3.2 on page 139). Revenue from sale of ROCs is recognised when the ROC is transferred to the account of a third party.

Revenue from the sale of electricity directly to business customers through our power retail business, Haven Power, is recognised on the supply of electricity when a contract exists, supply has taken place, a quantifiable price has been established or can be determined and the receivables are expected to be recovered at the point of sale. Energy supplied is measured based upon metered consumption and contractual rates; however where a supply has taken place but is not yet measured or billed, the revenue calculation is estimated based on consumption statistics and selling price estimates.

Revenues from the sale of wood pellets through our UK domestic pellet retail business, Billington Bioenergy are recognised at the point the pellets are delivered to the location specified in the contract, which is normally the customer's premises.

Other revenues derived from the provision of services (for example, the supply of ancillary generation services, such as black start and frequency response, to National Grid) are recognised by reference to the stage of completion of the contract. Most such contracts are for the delivery of a service either continually or on an ad-hoc basis over a period of time and thus stage of completion is calculated with reference to the amount of the contract term that has elapsed. Depending on the contract terms this approach may require judgement in enhancing probable future outcomes.

Other revenues derived from the sale of goods (for example, by-products from electricity generation such as ash and gypsum) are recognised at the point the risks and rewards of ownership pass to the customer, typically at the point of delivery to the customer's premises.

CfD payments

The Group is party to a Contract for Difference (CfD) with The Low Carbon Contracts Company (LCCC), a Government-owned entity responsible for delivering elements of the Government's Electricity Market Reform Programme. Under the contract, the Group makes or receives payments in respect of electricity dispatched from one of its three biomass-fuelled generating units. The payment is calculated with reference to a strike price of £100 per MWh. The strike price is in 2012 terms and increases each year indexed to UK CPI and system balancing costs. The strike price at 31 December 2016 was £106 per MWh.

Where market prices at the point of generation are above/below the strike price, the Group makes/receives an additional payment to/from LCCC equivalent to the difference between the market power price at the point of dispatch and the strike price. Such payments are in addition to amounts received from the sale of the power in the wholesale market and either increase or limit the total income from the power dispatched from the relevant generating unit to the strike price in the CfD contract.

The Group recognises the income or costs arising from the CfD in the income statement, as a component of revenue, at the point the flow of economic benefit becomes probable. This is considered to be the point at which the relevant generation is delivered and the payment becomes contractually due.

The Group began generating under the CfD contract on 21 December 2016 and, in accordance with this policy, accrued £10.3 million of revenue in respect of amounts due from the LCCC in the period ending 31 December 2016.

2.2 Revenue continued

ROC sales

The generation and sale of ROCs is a key driver of the Group's financial performance. The RO scheme started in April 2002 and places an obligation on electricity suppliers to source an increasing proportion of their electricity from renewable sources. Under the RO, ROCs are certificates issued to generators of renewable electricity which are then sold to suppliers to demonstrate they have fulfilled their obligations under the RO. ROCs are managed in compliance periods (CPs), running from April to March annually, CP1 commenced in April 2002. At 31 December 2016 we are in CP15.

To meet its obligations a supplier can either submit ROCs or pay the "buy-out" price at the end of the CP. The buy-out price was set at £30/ROC in CP1 and rises with inflation. ROCs are typically procured in arm's-length transactions with renewable generators at a market price typically slightly lower than the buy-out price for that CP. At the end of the CP, the amounts collected from suppliers paying the buy-out price form the "recycle fund", which is distributed on a pro-rata basis to ROC generators.

The financial benefit of a ROC recognised in the income statement at the point of generation is thus comprised of two parts: the expected value to be obtained in a sale transaction with a third party supplier and the expected recycle fund benefit to be received at the end of the CP. See note 3.2 on page 139 for further details of ROCs generated and sold by our Generation business and those utilised by our Retail business in the year.

Further analysis of our revenue for the year ending 31 December 2016 is provided in the table below:

	Year ended 31 December 2016		
	External £m	Intra-group £m	Total £m
Generation			
Power sales	1,193.4	686.5	1,879.9
ROC and LEC sales	366.7	181.7	548.4
CfD income	10.3	–	10.3
Ancillary services	47.3	–	47.3
Other income	5.0	–	5.0
Retail			
Power sales	1,319.6	–	1,319.6
Pellet sales	6.7	–	6.7
Other income	0.1	–	0.1
Biomass Supply			
Pellet sales	–	72.9	72.9
Other income	0.7	–	0.7
Elimination of intra-group sales	–	(941.1)	(941.1)
Total consolidated revenue	2,949.8	–	2,949.8

The Group's principal revenues arise from the sale of power, both into the wholesale market via Drax Power, our generation business, and to Industrial and Commercial and small and medium-sized enterprise business customers via Haven Power, our energy retail business. The Group also sells wood pellets into the domestic UK heat market via Billington Bioenergy, part of our retail business. Drax Biomass, our US-based wood pellet manufacturing business, generates all of its revenues intra-group, selling sustainable wood pellets to Drax Power to be used in the electricity generation process.

ROC sales and CfD income reflect revenues received through Government programmes to support renewable generation. ROC sales reflect consideration received for sales of ROCs by Drax Power to third parties. CfD income reflects amounts received under the CfD contract awarded by the UK Government to one of our biomass-fuelled electricity generation units. See CfD payments above for further details.

2.2 Revenue continued

The following is an analysis of the Group's revenues in the year ended 31 December 2015:

	Year ended 31 December 2015		
	External £m	Internal £m	Total £m
Generation			
Power sales	1,461.2	702.2	2,163.4
ROC and LEC sales	290.8	161.0	451.8
CfD income	–	–	–
Ancillary services	14.0	–	14.0
Other income	9.0	–	9.0
Retail			
Power sales	1,284.9	–	1,284.9
Pellet sales	4.6	–	4.6
Other income	0.5	–	0.5
Biomass Supply			
Pellet sales	–	28.1	28.1
Other income	–	0.3	0.3
Elimination of intra-group sales	–	(891.6)	(891.6)
Total consolidated revenue	3,065.0	–	3,065.0

2.3 Operating expenses and EBITDA

This note sets out the material components of "Operating and administrative expenses" in our Consolidated income statement, page 120, and a detailed breakdown of the fees we paid to our auditor, Deloitte LLP, in respect of services they provided to us during the year.

	Years ended 31 December	
	2016 £m	2015 £m
Gross profit	**376.3**	408.8
The following expenditure has been charged in arriving at operating profit/EBITDA:		
Staff costs (note 6.1)	**99.9**	106.8
Repairs and maintenance expenditure on property, plant and equipment	**68.9**	59.6
Other operating and administrative expenses	**67.5**	73.4
Total operating and administrative expenses	**236.3**	239.8
EBITDA	**140.0**	169.0

EBITDA is profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.

2.3 Operating expenses and EBITDA continued

Auditor's remuneration

	Years ended 31 December 2016 £000	2015 £000
Audit fees:		
Fees payable for the audit of the Group's consolidated financial statements	**448**	361
Fees payable for the audit of the Company's subsidiaries	**27**	74
	475	435
Other fees:		
Review of the Group's half-year condensed consolidated financial statements	**71**	70
Other services	**2**	2
Total audit related fees	**548**	507
Taxation services	**–**	7
Other assurance services	**610**	36
Total non-audit fees	**610**	43
Total auditor's remuneration	**1,158**	550

Other assurance services provided by Deloitte LLP in 2016 consist largely of reporting accountant services associated with the shareholder circular in relation to the Opus transaction, published on 18 January 2017. Non-audit services are approved by the Audit Committee in accordance with the policy set out on page 81.

2.4 Review of fixed assets for impairment

Accounting policy

The Group reviews its fixed assets (or, where appropriate, groups of assets known as cash-generating units (CGUs)) whenever there is an indication that an impairment loss may have been suffered. The Group considers the smallest collections of assets that generate independent cash flows to be its operating entities (Drax Power, Haven Power, Drax Biomass and Billington Bioenergy) and accordingly considers the Group to be comprised of four CGUs.

If an indication of potential impairment exists, the recoverable amount of the asset or CGU in question is assessed with reference to the present value of the future cash flows expected to be derived from the continuing use of the asset or CGU (value in use) or the expected price that would be received to sell the asset to another market participant (fair value). The initial assessment of recoverable amount is normally based on value in use.

Where value in use is calculated, the assessment of future cash flows includes all of the necessary costs expected to be incurred to generate the cash inflows from the CGU's assets in their current state and condition, including an allocation of centrally managed costs. Central costs are only allocated where they are necessary for and directly attributable to the CGU's activities. Future cash flows include, where relevant, contracted cash flows arising from our cash flow hedging activities and as a result, the carrying amount of each CGU includes the mark-to-market value of those cash flow hedges.

The additional value that could be obtained from enhancing or converting the Group's assets is not reflected, nor the potential benefit of any future restructuring or reorganisation. In determining value in use, the estimate of future cash flows is discounted to present value using a pre-tax rate.

If the recoverable amount is less than the current carrying amount in the financial statements, a provision is made to reduce the carrying amount of the asset or CGU to the estimated recoverable amount. Impairment losses are recognised immediately in the income statement.

Goodwill balances are assessed for impairment annually (see note 5.2).

Critical judgement areas

In 2015, the market capitalisation of the Group fell materially below the carrying value of the Group's net assets. Whilst the shortfall has reduced considerably during 2016, this remains the case at the balance sheet date. In addition, commodity markets are weak and the substantial weakening of Sterling against both the Euro and US dollar in the second half of 2016 indicated a potentially material increase in the long-term costs of fuel for our generation business, which are predominantly priced in these currencies. Accordingly an impairment review of the Drax Power CGU was undertaken at the balance sheet date. A review of other CGUs suggested no indicators of impairment.

2.4 Review of fixed assets for impairment continued

The assessment of the present value of future cash flows on which such a review is based is dependent upon a number of assumptions. In particular, expected future cash flows are based upon management's estimates of future prices, output, costs and economic support for renewable energy generation, including access to Capacity Market and Ancillary Services contracts. 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,

The most critical of these assumptions are discussed below.

Impairment review

The carrying amount of the Drax Power CGU at 31 December 2016 was £1,911 million. The value in use of the Drax Power CGU was tested using the Group's established planning model.

The analysis assumed that Drax Power's three biomass-fuelled generating units would continue in operation until the end of their estimated useful lives, currently considered to be 2039. In line with our assumption that coal-fired generation will cease by 2025, applied in light of the Government consultation published in November 2016, the three remaining coal-fired units were assumed to cease coal-fired generation by this date but will then be available for conversion to biomass-fired units. No account has been taken of any cash inflows that could result from such a conversion (which could take place earlier than 2025) in measuring the value in use of the Drax Power CGU.

The analysis depends on a broad range of assumptions, including the expected life of the six power generating units and the regulatory regime under which they might operate. The key assumptions (i.e. those most sensitive to a change, possibly resulting in a different outcome for impairment) are considered to be:

- The expected operating lives of the six generating units, as described above;
- Future commodity prices beyond the horizon of our existing contracted purchase and sale commitments – notably power prices and biomass prices;
- Future foreign exchange rates beyond the horizon of our existing contracted purchase commitments; and
- The continuance of existing biomass support regimes – CfD and RO – until 2027 and the existence of a favourable economic environment for biomass generation thereafter. This includes future Capacity Markets and Ancillary Services revenues.

These assumptions are all dependent on external market movements. The historic volatility in these assumptions is reflected in the financial performance of the Group but past performance is not necessarily a reliable indicator of future values.

Where available, estimates of future prices are based on signed contracts for purchases and sales with third parties. Transactions beyond contracted positions are valued using market data and forward price curves, based where possible on data points provided by a reputable third party source, independent to the Group. In particular, longer-term power prices are based on Department for Business, Energy and Industrial Strategy and National Grid assumptions. The contracted period for biomass purchases is substantially longer, with the longest-dated contracts expiring in 2027. Beyond this point, estimated biomass prices are largely based on our internal models and expectations for the biomass market.

Future foreign exchange rates are based on contracted foreign currency purchases to the extent possible. Beyond our contracted position, exchange rate estimates are based on market forward curves and, beyond this point, Bloomberg data.

Current Government plans for existing renewable support mechanisms, namely the CfD and RO, assume these cease in 2027. The impairment analysis made no assumptions regarding the direct replacement of these support mechanisms beyond this date. The biomass-fuelled units that are assumed to continue to generate power do so supported by the prevailing wholesale power price, delivery of ancillary services to the UK grid and an expectation that capacity market revenues would be available to these units. Our power price forecasts reflect increased volatility between peak and baseload prices. Assumed revenues from ancillary services and the capacity market are based on projections derived from current contracts and capacity market outcomes and how we expect the market to evolve. These assumptions reflect our expectation that Drax will be required to provide generation to support intermittent renewable power and be an essential part of the UK's energy mix throughout the life of the units.

The expected future cash flows were discounted using a pre-tax nominal rate of 8.4%. The discount rate is supported by observable market reports and independent analysis commissioned by, and specific to the circumstances of the Group. This indicated that the recoverable amount of the Drax Power CGU exceeded its carrying value with headroom of approximately £200 million and therefore that no provisions for impairment were required.

Sensitivity analysis indicated that, when compared to our base case assumptions, a reduction of approximately 7% in market power prices, an increase in biomass prices of approximately 11%, or a depreciation of Sterling against the US dollar of some 8% throughout the 23-year term of the valuation would result in a recoverable amount for the Drax Power CGU that is lower than its carrying amount. This does not consider the interaction effect of potential changes in several or all of the assumptions simultaneously, and the sensitivities do not take account of any mitigating actions that could be taken should the changes referred to materialise. In addition, in relation to central costs, no reasonable change in the method of allocation would result in an impairment charge.

2.5 Net finance costs

Finance costs reflect expenses incurred in managing our debt structure (such as interest payable on our bank loans) as well as foreign exchange gains and losses, the unwinding of discounting on provisions for reinstatement of our sites at the end of their useful lives (see note 5.3) and net interest charged on the Group's defined benefit pension scheme obligation (see note 6.3). These are offset by interest income that we generate through efficient use of short-term cash surpluses – for example through investment in money market funds.

	Years ended 31 December 2016 £m	2015 £m
Interest payable and similar charges:		
Interest payable on bank borrowings	**(19.4)**	(18.0)
Unwinding of discount on provisions (note 5.3)	**(4.5)**	(0.7)
Amortisation of deferred finance costs	**(2.1)**	(3.7)
Net finance cost in respect of defined benefit scheme (note 6.3)	**(0.9)**	(1.1)
Other financing charges	**(2.1)**	(0.8)
Total interest payable and similar charges	**(29.0)**	(24.3)
Interest receivable:		
Interest income on bank deposits	**0.6**	1.4
Total interest receivable	**0.6**	1.4
Foreign exchange gains	**22.0**	5.9
Net interest charge	**(6.4)**	(17.0)

Foreign exchange gains and losses recognised in interest arise on the retranslation of balances and investments denominated in foreign currencies to prevailing rates at the balance sheet date. Sterling weakened against the US dollar and Euro following the EU referendum in June, resulting in gains being recognised on assets the Group holds denominated in these currencies.

Amortisation of deferred finance costs for the previous period include £0.7 million relating to the previous revolving credit facility for which amortisation was accelerated following the successful renegotiation of a replacement facility in December 2015.

2.6 Current and deferred taxation

The tax charge includes both current and deferred tax. Current tax is the estimated amount of tax payable on this year's taxable profits (which are adjusted for items upon which we are not required to pay tax or, in some cases, for items which are not allowable for tax purposes and therefore on which we are required to pay additional tax). Deferred tax is an accounting adjustment which reflects where more or less tax is expected to arise in the future due to differences between the accounting and tax rules (reflected in differences between the carrying amounts of assets and liabilities in the balance sheet and the corresponding tax bases used in the computation of taxable profits). The tax charge reflects the estimated effective tax rate on profit before tax for the Group for the year ended 31 December 2016 and the movement in the deferred tax balance in the year, so far as it relates to items recognised in the income statement.

Accounting policy

Current tax, including UK corporation tax and foreign tax, is based on the taxable profit or loss for the year in the relevant jurisdiction. Taxable profit or loss differs from profit/loss before tax as reported in the income statement because it excludes items of income or expenditure that are either taxable or deductible in other years or never taxable/deductible. The 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. 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 jurisdictional tax laws and rates that have been enacted or substantively enacted at the balance sheet date. In the UK 2016 Budget, the UK Government proposed a reduction in the rate of UK corporation tax from 18% to 17% from 1 April 2020. This change was enacted into law in September 2016 and accordingly these rates have been reflected in the UK deferred tax balance at 31 December 2016.

Current and deferred tax are recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are recognised in other comprehensive income or directly in equity respectively.

2.6 Current and deferred taxation continued

Significant judgement areas

In accounting for taxation the Group makes assumptions regarding the treatment of items of income and expenditure for tax purposes. The Group believes that these 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. Where such assets relate to losses incurred by a business unit, particularly one with a history of losses, the Group seeks evidence other than its own internal forecasts to support recognition of the related deferred tax asset.

	Years ended 31 December	
	2016 £m	2015 £m
Tax charge comprises:		
Current tax	8.5	1.8
Deferred tax		
– Before impact of corporation tax rate change	4.5	18.7
– Impact of corporation tax rate change	(9.8)	(17.8)
Tax charge	3.2	2.7

	Years ended 31 December	
	2016 £m	2015 £m
Tax charged on items recognised in other comprehensive income:		
Deferred tax on actuarial gains on defined benefit pension scheme (note 6.3)	(1.6)	0.2
Deferred tax on cash flow hedges (note 7.4)	59.6	4.9
	58.0	5.1

UK corporation tax is the main rate of tax for the Group and is calculated at 20% (2015: 20.25%) of the estimated assessable profit for the year. Tax for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions. The tax charge for the year can be reconciled to the profit per the income statement as follows:

	Years ended 31 December	
	2016 £m	2015 £m
Profit before tax	197.1	59.0
Profit before tax multiplied by the rate of corporation tax in the UK of 20% (2015: 20.25%)	39.4	11.9
Effects of:		
Adjustments in respect of prior periods	(3.6)	1.5
Expenses not deductible for tax purposes	1.7	0.9
Impact of change to corporation tax rate	(9.8)	(17.8)
Difference in overseas tax rates and other benefits	(4.8)	–
Deferred tax on prior year start up losses and other temporary differences	(21.4)	–
Other	1.7	6.2
Total tax charge	3.2	2.7

The Adjustments in respect of prior periods principally relates to a research and development claim which was successfully concluded with HMRC during the period. In 2015 Other items included the US losses which were not recognised for deferred tax purposes in that year.

2.6 Current and deferred taxation continued

The movements in deferred tax assets and liabilities during each year are shown below.

Deferred tax (liabilities)/assets

	Financial instruments £m	Accelerated capital allowances £m	Non-trade losses £m	Trade losses £m	Other liabilities £m	Other assets £m	Total £m
At 1 January 2015	22.5	(198.4)	7.6	–	(26.6)	9.0	(185.9)
Credited/(charged) to the income statement	(24.9)	35.9	(6.1)	–	(4.3)	(1.5)	(0.9)
Charged to equity in respect of actuarial gains	–	–	–	–	–	(0.2)	(0.2)
Charged to equity in respect of cash flow hedges	(4.9)	–	–	–	–	–	(4.9)
At 1 January 2016	(7.3)	(162.5)	1.5	–	(30.9)	7.3	(191.9)
(Charged)/credited to the income statement	**(33.9)**	**(7.1)**	**(1.5)**	**35.3**	**5.3**	**7.2**	**5.3**
Charged to equity in respect of actuarial gains	–	–	–	–	–	**1.6**	**1.6**
Charged to equity in respect of cash flow hedges	**(59.6)**	–	–	–	–	–	**(59.6)**
Effect of changes in foreign exchange rates	–	(1.3)	–	3.5	–	0.7	**2.9**
At 31 December 2016	**(100.8)**	**(170.9)**	–	**38.8**	**(25.6)**	**16.8**	**(241.7)**
Deferred tax balances (after offset) for financial reporting purposes:							
Net deferred tax asset	–	**(14.4)**	–	**38.8**	–	**9.1**	**33.5**
Net deferred tax liability	**(100.8)**	**(156.5)**	–	–	**(25.6)**	**7.7**	**(275.2)**

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to do so, otherwise are shown separately in the balance sheet.

In the period the Group recognised a net deferred tax asset valued at £34 million in respect of start-up losses and other temporary differences in the US-based Drax Biomass business (£21 million of this asset relates to losses that arose in previous years). Recognition in 2016 reflects an improvement in operational performance and the Board's increased confidence regarding the delivery of future taxable profits against which the losses will be utilised currently expected by 2027. As a one-off and non-cash item, this credit has been excluded from the calculation of underlying earnings and the dividend for 2016 (see notes 2.7 and 2.8). These start-up losses are valued at the US Federal tax rate as was enacted at the balance sheet date (35%). Should Federal tax rates reduce/increase in the future, this will correspondingly reduce/increase (respectively) this net deferred tax asset.

The Group has not recognised deferred tax assets with an estimated value of £2 million at 31 December 2016 (2015: £2 million), in respect of UK losses totalling £12 million, that are carried forward against future taxable income. The business unit involved has a history of making losses and until sufficient operational performance is established and maintained to give suitable confidence in future profitability, taxable income against which to utilise the benefit of the accumulated losses is not considered to be probable.

2.7 Earnings per share and underlying earnings per share

Earnings per share (EPS) represents the amount of our earnings (post-tax profits) that is attributable to each ordinary share we have in issue. Basic EPS is calculated by dividing our earnings (profit after tax calculated in accordance with IFRS) by the weighted average number of ordinary shares that were in issue during the year. Diluted EPS demonstrates the impact if all outstanding share options (such as those to be issued under our employee share schemes – see note 6.2), that are expected to vest on their future maturity dates, were exercised and treated as ordinary shares as at the balance sheet date.

In addition to EPS, we calculate underlying EPS as it reflects the figures upon which our annual dividends are calculated (note 2.8). Underlying EPS removes the post-tax effect of unrealised gains and losses on derivative contracts, plus particular transactions considered to be one-off in nature that do not reflect the underlying trading performance of the Group, from post-tax profits. Multiplying underlying basic EPS by 50% will give the total dividends per share for the period.

2.7 Earnings per share and underlying earnings per share continued

The table below reconciles earnings, calculated in accordance with IFRS, to underlying profit after tax:

	Years ended 31 December 2016 £m	2015 £m
Earnings:		
Earnings attributable to equity holders of the Company for the purposes of basic and diluted earnings	**193.9**	56.3
Adjusted for:		
Unrealised gains on derivative contracts	**(176.8)**	(123.7)
Asset obsolescence charges	**–**	109.2
Tax impact of the above items	**33.9**	4.2
Deferred tax on start-up losses and other temporary differences	**(30.5)**	–
Underlying profit after tax attributable to equity holders of the Company	**20.5**	46.0

The effect of potentially dilutive options on the weighted average number of shares in issue at the balance sheet date is shown below:

	Years ended 31 December 2016	2015
Number of shares:		
Weighted average number of ordinary shares for the purposes of basic earnings per share (millions)	**406.6**	406.0
Effect of dilutive potential ordinary shares under share plans	**2.7**	1.3
Weighted average number of ordinary shares for the purposes of diluted earnings per share (millions)	**409.3**	407.3

Earnings per share – basic (pence)	**48**	14
Earnings per share – diluted (pence)	**47**	14
Underlying earnings per share – basic (pence)	**5**	11
Underlying earnings per share – diluted (pence)	**5**	11

2.8 Dividends

Dividends are amounts we return to our shareholders and are paid as an amount per ordinary share held. Our current dividend policy is to return 50% of underlying profit after tax (see note 2.7) to our shareholders each year. The remaining 50% is retained for reinvestment in the business.

	Years ended 31 December 2016 £m	2015 £m
Amounts recognised as distributions to equity holders in the year (based on the number of shares in issue at the record date):		
Interim dividend for the year ended 31 December 2016 of 2.1 pence per share paid on 7 October 2016 (2015: 5.1 pence per share paid on 9 October 2015)	**8.6**	20.7
Final dividend for the year ended 31 December 2015 of 0.6 pence per share paid on 13 May 2016 (2015: 7.2 pence per share paid on 15 May 2015)	**2.4**	29.2
	11.0	49.9

At the forthcoming Annual General Meeting the Board will recommend to shareholders that a resolution is passed to approve payment of a final dividend for the year ended 31 December 2016 of 0.4 pence per share (equivalent to approximately £1.8 million) payable on or before 12 May 2017. The final dividend has not been included as a liability as at 31 December 2016.

2.9 Retained profits

Retained profits are a component of our equity reserves. The overall balance reflects the total profits we have generated over our lifetime, reduced by the amount of that profit we have distributed to our shareholders. The table below sets out the movements in our retained profits during the year.

	Years ended 31 December	
	2016 £m	2015 £m
At 1 January	**385.2**	372.5
Profit for the year	**193.9**	56.3
Actuarial (losses)/gains on defined benefit pension scheme (note 6.3)	**(8.4)**	1.2
Deferred tax on actuarial (losses)/gains on defined benefit pension scheme (note 2.6)	**1.6**	(0.2)
Equity dividends paid (note 2.8)	**(11.0)**	(49.9)
Net movements in equity associated with share-based payments (note 6.2)	**5.2**	5.3
At 31 December	**566.5**	385.2

Distributable profits

The capacity of the Group to make dividend payments is primarily determined by the availability of retained distributable profits and cash resources.

The immediate cash resources of the Group of £228.4 million are set out in note 4.2 and the recent history of cash generation within note 4.4. The majority of these cash resources are held by the principal operating subsidiaries of the Group, in particular Drax Power Limited.

The Parent Company financial statements, set out on pages 167 to 172 of this report, disclose the Parent Company's distributable reserves of £229 million. The Group has, relative to previous dividend payments (note 2.8), sufficient retained profits, which are accessible by the Parent Company, for future distributions in accordance with the Group's dividend policy.

SECTION 3:

OPERATING ASSETS AND WORKING CAPITAL

This section gives further information on the operating assets we use to generate revenue and the short-term liquid assets and liabilities, managed during day-to-day operations, that comprise our working capital balances.

3.1 Property, plant and equipment

This note shows the cost, depreciation and net book value of the physical assets controlled by us that we use in our businesses to generate revenue. The cost of an asset is what we paid to purchase or construct the asset. Depreciation reflects the usage of the asset over time and is calculated by taking the cost of the asset, net of any residual value, to the income statement evenly over the useful economic life of the asset. An asset's net book value is its cost less any depreciation (including impairment, if required) charged to date.

Additions in 2016 include a further £29 million (2015: £90 million) on our biomass transformation project, which is now largely complete and in line with initial expectations on timing and overall cost. At Drax Power Station we now have three fully converted units running on biomass fuel, the third of which completed its conversion following the award of the CfD in December 2016. Upstream, in our US-based wood pellet manufacturing business, both pellet plant facilities and the port facility ran commercial operations for the first full year.

Accounting policy

Property, plant and equipment are initially measured at cost. Cost comprises the purchase price (after deducting trade discounts and rebates), any 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, and the estimate of the present value of the costs of dismantling and removing the item and restoring the site. Property, plant and equipment are stated at cost less accumulated depreciation and any provision for impairment in value.

We construct many of our assets as part of long-term development projects. Assets that are in the course of construction are not depreciated until they are ready for us to use in the way intended.

Depreciation is provided on a straight-line basis to write down assets to their residual value evenly over the estimated useful lives (UEL) of the assets from the date of acquisition (where relevant, limited to the expected decommissioning date of the power station – currently expected to be 2039). The table below shows the range of useful lives at the date of acquisition and the average remaining useful life at the balance sheet date of the main categories of asset we own in years:

	Average UEL remaining	Range of UELs
Freehold buildings	23	8–32
Plant and equipment		
Electricity generation plant	19	3–32
Biomass specific assets	21	4–26
Coal specific assets	23	3–32
Pellet production plant	19	5–20
Other plant, machinery and equipment	15	2–30
Decommissioning asset	23	35
Plant spare parts	23	Up to 35

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

Electricity generation plant refers to core electricity generation assets at Drax Power Station which are fuel agnostic. Biomass-specific and coal-specific assets are those assets that are only necessary to support electricity generation from the specified fuel and include fuel storage and distribution systems.

Within the plant and equipment categories shorter lives are attributed to components that are overhauled and upgraded as part of rolling outage cycles. The majority of assets within these categories have a remaining useful life in excess of 15 years.

Plant spare parts are depreciated over the remaining useful life of the power station.

Costs relating to major inspections, overhauls and upgrades to the power station are included in the asset's carrying amount or recognised as a separate asset, as appropriate, if the recognition criteria are met; namely, when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed as incurred.

Estimated useful lives and residual values are reviewed annually, taking into account regulatory change and commercial and technological obsolescence as well as normal wear and tear. Residual values are based on prices prevailing at each balance sheet date. Any changes are applied prospectively.

3.1 Property, plant and equipment continued

Critical judgement areas

The carrying values of property, plant and equipment are reviewed for impairment where there has been a trigger event (that is, an event which may have resulted in impairment) by assessing the present value of estimated future cash flows and net realisable value compared with net book value. The calculation of estimated future cash flows and residual values is based on management's reasonable estimates of future prices, output and costs, and is therefore subjective. Estimated useful lives are based on past experience, future replacement cycles and other available evidence; however an inherent degree of judgement remains.

Asset lives are reviewed annually at each balance sheet date. As part of the most recent annual review of asset lives, the estimated useful life of coal-specific assets at Drax Power Station will be revised with effect from 1 January 2017. On 9 November 2016 the Government announced a consultation on the future closure of unabated coal-fired generation. Having considered this event, management concluded that coal generation will cease during 2025, but that the three coal units will be retained for conversion to biomass-fuelled generation in the period to 2039. This results in the shortening to 2025 of the useful lives of the coal-specific assets which will not be required to support generation after this date. This change is applied prospectively, from the point of management's decision, and will result in an increase of approximately £27 million per annum in depreciation charges from 1 January 2017 to 31 December 2025.

The useful lives of electricity generation plant currently fuelled by coal are unaffected by this change. These assets can be utilised using alternative fuel sources without material modification.

At each balance sheet date the Group reviews its property, plant and equipment to determine whether there is any indication that these assets may be impaired. Accounting policies in respect of impairment, along with details of the impairment review conducted during 2016, are set out in note 2.4.

	Freehold land and buildings £m	Plant and equipment £m	Plant spare parts £m	Total £m
Cost:				
At 1 January 2015	248.8	2,059.8	55.8	2,364.4
Additions at cost	90.7	69.4	13.7	173.8
Disposals	(11.9)	(38.5)	–	(50.4)
Issues/transfers	(9.5)	20.6	(11.0)	0.1
At 1 January 2016	318.1	2,111.3	58.5	2,487.9
On acquisition (note 5.1)	**1.3**	**0.2**	**–**	**1.5**
Additions at cost	**0.8**	**84.3**	**10.6**	**95.7**
Disposals	**(7.2)**	**(28.1)**	**–**	**(35.3)**
Issues/transfers	**(11.9)**	**19.0**	**(4.5)**	**2.6**
Effect of foreign currency exchange differences	**0.7**	**1.1**	**–**	**1.8**
At 31 December 2016	**301.8**	**2,187.8**	**64.6**	**2,554.2**
Accumulated depreciation and impairment:				
At 1 January 2015	57.9	594.3	15.0	667.2
Obsolescence charges	0.1	109.1	–	109.2
Depreciation charge for the year	8.1	90.8	1.5	100.4
Disposals	(11.7)	(31.4)	0.4	(42.7)
At 1 January 2016	54.4	762.8	16.9	834.1
Depreciation charge for the year	**11.2**	**96.7**	**1.6**	**109.5**
Disposals	**(6.5)**	**(25.0)**	**–**	**(31.5)**
Effect of foreign currency exchange differences	0.2	0.4	–	0.6
At 31 December 2016	**59.3**	**834.9**	**18.5**	**912.7**
Net book amount at 31 December 2015	263.7	1,348.5	41.6	1,653.8
Net book amount at 31 December 2016	**242.5**	**1,352.9**	**46.1**	**1,641.5**

Assets in the course of construction amounted to £120.5 million at 31 December 2016 (2015: £217.0 million). Additions to assets in the course of construction were £88.6 million in 2016.

3.1 Property, plant and equipment continued

Plant and equipment includes assets held under finance lease agreements with a carrying value at 31 December 2016 of £1.6 million (2015: £1.6 million).

Additions during the year include £nil (2015: £1.9 million) of capitalised borrowing costs directly attributable to the construction of specific assets.

3.2 ROC and LEC assets

We earn ROC assets, which are accredited by the Office for Gas and Electricity Markets ("Ofgem"), as a result of burning sustainable compressed wood pellets to generate electricity. This note sets out the value of these assets that we have earned but not yet sold.

As we generate more of our electricity by burning sustainable compressed wood pellets, the volume and therefore the total value of ROC assets we have generated has increased. With the approval of the CfD in December 2016, total ROC generation is expected to reduce in 2017. Haven Power provides us with a credit-efficient and timely route to market for these ROCs, as do the ROC monetisation facilities described in note 7.1.

Following the Government's decision to remove the Climate Change Levy exemption for power generated from renewable sources, as of 1 August 2015 we no longer earn LECs for electricity generated from sustainable compressed wood pellets.

Accounting policy

ROCs are recognised as current assets in the period they are generated and are initially measured at fair value based on anticipated sales prices. The value of ROCs earned is recognised in the income statement as a reduction in fuel costs in that period.

Where our retail activities incur an obligation to deliver ROCs to Ofgem, that obligation is provided for in the period incurred.

At each reporting date the Group reviews the fair value of ROC assets generated but not sold against updated anticipated sales prices including, where relevant, agreed forward sale contracts and taking into account likely utilisation of ROCs generated to settle our own ROC obligations. Any impairments required are recognised in the income statement in the period incurred.

Critical judgement areas

The fair values and net realisable values of ROCs referred to above are calculated with reference to assumptions regarding future sales prices in the market, taking into account agreed forward sale contracts where appropriate. Historic experience indicates that the assumptions used in the valuation are reasonable; however actual sales prices may differ from those assumed.

ROC valuations also include an estimate of the future benefit that may be obtained from the ROC recycle fund at the end of the compliance period. The recycle fund provides a benefit where Supplier buy-out charges (incurred by Suppliers who do not procure sufficient ROCs to satisfy their obligations) are returned to renewable generators on a pro-rata basis. The estimate is based on assumptions about likely levels of renewable generation and supply over the compliance period and is thus subject to some uncertainty. The Group utilises external sources of information in addition to its own forecasts in calculating these estimates. Past experience indicates that the values arrived at are reasonable but they remain subject to possible variation.

	ROCs £m	LECs £m	Total £m
Fair value and carrying amount:			
At 1 January 2015	173.8	10.7	184.5
Earned from generation	482.1	34.0	516.1
Purchased from third parties	16.4	3.8	20.2
Utilised by our retail business/sold to third parties	(406.6)	(44.1)	(450.7)
At 1 January 2016	265.7	4.4	270.1
Earned from generation	**535.8**	–	**535.8**
Utilised by our retail business/sold to third parties	**(543.9)**	**(4.4)**	**(548.3)**
At 31 December 2016	**257.6**	–	**257.6**

Recognition of revenue from sales of ROCs and LECs is described in further detail on page 128.

3.3 Inventories

We hold stocks of fuels and other consumable items that we use in the process of generating electricity, and raw materials used in the production of compressed wood pellets. This note shows the cost of coal, biomass, other fuels and plant consumables that we held at the end of the year, including items at Drax Power Station, our facilities in the US and those owned by us but stored in off-site locations.

Accounting policy

Our raw materials and fuel stocks are valued at the lower of the weighted average cost to purchase and net realisable value.

The cost of fuel stocks includes all direct costs and overheads incurred in bringing the fuel to its present location and condition, including the purchase price, import duties and other taxes (including amounts levied on coal under the UK carbon price support mechanism) and transport/handling costs.

Critical judgement areas

Whilst value is largely based on observable costs, given the storage and handling characteristics of coal and biomass, an element of judgement is inherent in calculating the volume of fuel stocks owned by the Group at any given time.

Both coal and biomass stocks are weighed when entering, moving around or exiting sites using technology regularly calibrated to industry standards. Fuel burn in the electricity generation process is calculated using a combination of weights and thermal efficiency calculations to provide closing stock volumes. Both calibrated weighers and efficiency calculations are subject to a range of tolerable error.

Coal stocks are verified by an independent stock survey carried out by a suitably trained specialist, and a provision is made where the survey indicates a lower level of stock than indicated by the methods described above. Despite being an independent process, the survey depends on estimates and assumptions and as a result actual values may differ.

The characteristics of biomass require specialist handling and storage. On-site biomass is stored in sealed domes with a carefully controlled atmosphere for fire prevention purposes. Biomass stock is surveyed using regularly calibrated state-of-the-art RADAR scanning technology. However, this survey remains subject to a tolerable error range.

Experience indicates that the estimates and assumptions made by management in calculating stock volumes are reasonable. However, actual values may differ from initial calculations.

	As at 31 December	
	2016 £m	2015 £m
Coal	**66.4**	89.4
Biomass	**197.5**	118.7
Other fuels and consumables	**23.6**	15.9
	287.5	224.0

Inventories of biomass include £2.3 million of fibre and other raw materials utilised in the production of compressed wood pellets (2015: £2.0 million) and £2.0 million of work in progress (2015: £1.8 million) in our biomass supply business.

The cost of inventories recognised as an expense in the year ended 31 December 2016 was £1,173.5 million (2015: £1,306.9 million).

3.4 Trade and other receivables

Trade receivables represent amounts owed to us by our customers for goods or services we have provided but not yet been paid for. Other receivables include accrued income, which is income earned in the period but not yet invoiced, largely in respect of power delivered that will be invoiced the following month, and prepayments, which are amounts paid by the Group for which we are yet to receive the relevant goods or services in return (e.g. insurance premiums relating to periods after the balance sheet date).

Accounting policy

Trade and other receivables, given their short tenor, are measured at cost. A provision for impairment of trade receivables is established where there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivable.

3.4 Trade and other receivables continued

	As at 31 December 2016 £m	2015 £m
Amounts falling due within one year:		
Trade receivables	**87.0**	99.5
Accrued income	**100.0**	157.0
Prepayments and other receivables	**105.9**	62.8
	292.9	319.3

Trade receivables principally represent sales of electricity to counterparties within both our generation and retail businesses. At 31 December 2016, the Group had amounts receivable from four (2015: two) significant counterparties within the generation business, representing 46% (2015: 41%) of trade receivables, both of which paid within 15 days of receipt of invoice in line with agreed terms.

Of total trade receivables at 31 December 2016, £33.4 million (2015: £41 million) relates to retail power sales. The risk profile of retail debt is different from that of the generation business with a larger volume of counterparties, and hence a lower concentration of credit risk, with different payment terms. All past-due receivables are assessed against the Group's credit risk policies for indicators of impairment and provisions made where appropriate. The value of retail debts that are past-due and not provided against, in accordance with this assessment, is not material.

Accordingly, management does not consider there to be any requirement for further provisions in excess of the normal provision for doubtful debts of £4.0 million (2015: £4.9 million). This provision, which largely relates to retail receivables, has been determined with reference to past default experiences in line with our policies. Credit and counterparty risk are both discussed in further detail in note 7.1.

The movement in the allowance for doubtful debts is laid out in the following table:

	Years ended 31 December 2016 £m	2015 £m
At 1 January	**4.9**	6.8
Receivables written off	**(3.3)**	(5.0)
Provision for receivables impairment	**2.4**	3.1
At 31 December	**4.0**	4.9

3.5 Trade and other payables

Trade and other payables represent amounts we owe to our suppliers (for goods and services provided), tax authorities and other creditors that are due to be paid in the ordinary course of business. We make accruals for amounts that will fall due for payment in the future as a result of our activities in the current year (e.g. fuel we have received but for which we have not yet been invoiced).

Accounting policy

Trade and other payables, given their short tenor, are measured at cost.

	As at 31 December 2016 £m	2015 £m
Amounts falling due within one year:		
Trade payables	**87.4**	41.7
Fuel accruals	**77.6**	131.4
Other accruals	**341.7**	260.8
Other payables	**62.1**	54.1
Amounts payable for acquisitions (note 5.1)	**23.1**	–
	591.9	488.0

Other accruals includes £166 million (2015: £133 million) in relation to the Group's obligation to deliver ROCs arising from its Retail activities.

The Group recognises a liability in respect of its unsettled obligations to deliver emissions allowances under the EU Emission Trading Scheme (ETS). Accruals at 31 December 2016 include £2.8 million (2015: £10.0 million) with respect to the Group's estimated net liability to deliver CO_2 emissions allowances. Allowances are purchased in the market and are recorded at cost.

SECTION 4:

FINANCING AND CAPITAL STRUCTURE

This section gives further information regarding the Group's capital structure (equity and debt financing) and cash generated from operations during the year.

4.1 Reconciliation of net debt

Net debt is calculated by taking our borrowings (note 4.3) and subtracting cash and cash equivalents (note 4.2). The table below reconciles net debt in terms of changes in these balances across the year.

	Years ended 31 December	
	2016 £m	2015 £m
Net debt at 1 January	**(186.6)**	(98.6)
Increase/(decrease) in cash and cash equivalents	**86.7**	(49.0)
(Decrease)/increase in short-term investments	**–**	(40.1)
Increase in borrowings	**(1.5)**	(0.8)
Effect of changes in foreign exchange rates	**7.9**	1.9
Net debt at 31 December	**(93.5)**	(186.6)

The increase in borrowings reflects the accrual of interest on the Group's term loans (see note 4.3).

4.2 Cash and cash equivalents

Cash and cash equivalents include cash held in current and other deposit accounts that are accessible on demand. It is our policy to invest available cash on hand in short-term, low risk bank or building society deposits.

	As at 31 December	
	2016 £m	2015 £m
Cash and cash equivalents	**228.4**	133.8

4.3 Borrowings

Our financing structure includes £325 million of term loans, comprised of a private placement of £100 million with various funds managed by M&G Investments, a £75 million amortising loan facility with Friends Life, underpinned by a guarantee from HM Treasury under the Infrastructure UK Guarantee Scheme, a £50 million amortising term loan with Green Investment Bank and a £100 million amortising term loan facility with M&G UK Companies Financing Fund. The loans have varying maturity profiles ranging from 2017 to 2025. All of the term loans were fully drawn down at 31 December 2016 and 31 December 2015.

In addition, the Group has access to a £400 million revolving credit facility (RCF). The facility matures in December 2019 and has a margin of 175 basis points over LIBOR. At 31 December 2016 this facility had been utilised to draw down letters of credit with a total value of £57.9 million (2015: £37.9 million) (see note 7.5).

The Group also has a commodity trading facility, which allows us to transact prescribed volumes of commodity trades without the requirement to post collateral.

Accounting policy

The Group measures all debt instruments (whether financial assets or financial liabilities) initially at fair value, which equates to the principal value of the consideration paid or received. Subsequent to initial measurement, debt instruments are measured at amortised cost using the effective interest method. Transaction costs (any such costs incremental and directly attributable to the issue of the financial instrument) are included in the calculation of the effective interest rate and are amortised through the income statement over the life of the instrument.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. Where this is the case, the fee is deferred until the draw-down occurs.

Analysis of borrowings

Borrowings at 31 December 2016 and 31 December 2015 consisted principally of amounts drawn down against bank loans.

4.3 Borrowings continued

	As at 31 December 2016		
	Borrowings before deferred finance costs £m	Deferred finance costs £m	Net borrowings £m
Term loans	**327.9**	**(7.1)**	**320.8**
Finance lease liabilities	**1.1**	**–**	**1.1**
Total borrowings	**329.0**	**(7.1)**	**321.9**
Less current portion	**(37.9)**	**2.0**	**(35.9)**
Non-current borrowings	**291.1**	**(5.1)**	**286.0**

	As at 31 December 2015		
	Borrowings before deferred finance costs £m	Deferred finance costs £m	Net borrowings £m
Term loans	328.4	(8.9)	319.5
Finance lease liabilities	0.9	–	0.9
Total borrowings	329.3	(8.9)	320.4
Less current portion	(0.3)	–	(0.3)
Non-current borrowings	329.0	(8.9)	320.1

The term loans and RCF are guaranteed and secured by a number of the Group's subsidiary undertakings that are party to the security arrangement.

Post balance sheet event
The acquisition of Opus Energy Group Limited on 10 February 2017 (see note 5.1) was partially financed by a new acquisition loan facility of £375 million. At the date of approval of these financial statements, £200 million of this facility had been drawn down. The facility is unsecured and matures in July 2018.

4.4 Cash generated from operations

Cash generated from operations is the starting point of our cash flow statement on page 124. The table below makes adjustments for any non-cash accounting items to reconcile our net profit for the year to the amount of cash we have generated from our operations.

	Years ended 31 December	
	2016 £m	2015 £m
Profit for the year	**193.9**	56.3
Adjustments for:		
Interest payable and similar charges	**7.0**	18.4
Interest receivable	**(0.6)**	(1.4)
Tax charge	**3.2**	2.7
Depreciation	**109.5**	100.4
Asset obsolescence charges	**–**	109.2
Losses on disposal	**3.8**	7.1
Unrealised gains on derivative contracts	**(176.8)**	(123.7)
Defined benefit pension scheme current service cost	**6.0**	6.4
Non-cash charge for share-based payments	**5.2**	5.3
Close out of currency contracts[1]	**14.0**	–
Operating cash flows before movement in working capital	**165.2**	180.7
Changes in working capital:		
(Increase)/decrease in inventories	**(63.5)**	18.0
Decrease in receivables	**28.6**	48.9
Increase in payables	**73.7**	26.8
Decrease/(increase) in carbon assets	**11.1**	(11.8)
Decrease/(increase) in ROC and LEC assets	**12.5**	(85.6)
Total cash released from working capital	**62.4**	(3.7)
Defined benefit pension scheme contributions	**(14.5)**	(11.0)
Cash generated from operations	**213.1**	166.0

Note:
1 During 2016 we closed out a number of in-the-money forward foreign currency purchase contracts. As these contracts were designated into hedge accounting relationships under IAS 39, the benefit is being recognised in the income statement in the period the hedged transaction occurs.

4.5 Equity and reserves

Our ordinary share capital reflects the total number of shares in issue, which are publicly traded on the London Stock Exchange.

Accounting policy

Ordinary shares are classified as equity as evidenced by their residual interest in the assets of the Company after deducting its liabilities. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

	As at 31 December	
	2016 £m	2015 £m
Authorised:		
865,238,823 ordinary shares of $11^{16}/_{29}$ pence each	**100.0**	100.0
Issued and fully paid:		
2016 – 406,700,321 ordinary shares of $11^{16}/_{29}$ pence each	**47.0**	46.9
	47.0	46.9

4.5 Equity and reserves continued

The movement in allotted and fully paid share capital of the Company during the year was as follows:

	Years ended 31 December	
	2016 (number)	2015 (number)
At 1 January	**406,317,162**	404,821,561
Issued under employee share schemes	**383,159**	1,495,601
At 31 December	**406,700,321**	406,317,162

The Company has only one class of shares, which are ordinary shares of $11^{16}/_{29}$ pence each, carrying no right to fixed income. No shareholders have waived their rights to dividends.

Shares issued under employee share schemes

On 6 January a total of 30,081 shares were issued on early vesting of the Group's Bonus Matching Plan (BMP) by one individual whose employment had terminated and discretion was used to vest the shares. On 29 February 335,856 shares were issued in satisfaction of shares vesting in accordance with the rules of the Group's BMP. Throughout May to December a total of 17,222 shares were issued in satisfaction of options vesting in accordance with the rules of the Group's Savings-Related Share Option Plan.

Translation reserve

Exchange differences relating to the translation of the net assets of the Group's US-based subsidiaries from their functional currency (US dollar) into sterling for presentation in these consolidated accounts, are recognised in the translation reserve.

	Years ended 31 December	
	2016 £m	2015 £m
At 1 January	**(1.1)**	1.8
Exchange differences on translation of foreign operations	**(9.1)**	(2.9)
At 31 December	**(10.2)**	(1.1)

Other reserves

The share premium account reflects amounts received in respect of issued share capital that exceed the nominal value of the shares issued.

Other equity reserves reflect the impact of certain historical transactions, which are described under the table below.

	Capital redemption reserve		Share premium		Merger reserve	
	2016 £m	2015 £m	**2016 £m**	2015 £m	**2016 £m**	2015 £m
At 1 January	**1.5**	1.5	**424.2**	422.8	**710.8**	710.8
Issue of share capital	**–**	–	**–**	1.4	**–**	–
At 31 December	**1.5**	1.5	**424.2**	424.2	**710.8**	710.8

The capital redemption reserve arose when the Group completed a share buy-back programme in 2007.

The share premium and the merger reserve arose on the financial restructuring of the Group which took place in 2005.

Movements in the hedge reserve, which reflect the change in fair value of derivative financial instruments designated into hedge accounting relationships in accordance with IFRS, are set out in note 7.4.

SECTION 5:

OTHER ASSETS AND LIABILITIES

This section provides information on the assets and liabilities in the Consolidated balance sheet that are not covered in other sections, including goodwill, other intangible assets and the provision for reinstatement.

5.1 Acquisitions

Accounting policy

Acquisitions of subsidiaries and businesses are recognised at the point the Group obtains control of the target (the acquisition date). The consideration transferred and the assets and liabilities acquired are measured at their fair value on the acquisition date. The assets and liabilities acquired are recognised in the Consolidated balance sheet and the profits of the acquired business are recognised in the Consolidated income statement from the acquisition date. Acquisition-related costs are recognised in the income statement in the period the acquisition occurs. Goodwill is measured as the excess of the fair value of the consideration transferred over the fair value of the identifiable net assets acquired.

Acquisitions in the financial year

The transactions in this section occurred in the year ended 31 December 2016 and are reflected in the consolidated financial statements.

Acquisition of four OCGT development projects

On 6 December 2016 the Group acquired 100% of the issued share capital of Progress Power Limited (PPL), Hirwaun Power Limited (HPL), Millbrook Power Limited (MPL) and Abergelli Power Limited (APL). PPL, HPL, MPL and APL each hold a proposed development option, on land located in England and Wales, for a 299MW Open-Cycle Gas Turbine (OCGT) project. Both PPL and HPL have obtained Development Consent Orders for their sites. The acquisitions represent diversification of our generation capability in response to the changing energy requirements of the UK.

Initial consideration of £18.6 million was settled in cash on 3 January 2017, with the amount held as a liability in the balance sheet at 31 December 2016. The final purchase price depends upon future clearing prices in T-4 capacity market auctions from 2016–2020. The range of possible outcomes being zero further consideration if the capacity market clearing price does not exceed £28/KW in these auctions, with a maximum contingent consideration payable of £72 million, based on a clearing price of £75/KW. The fair value of the contingent consideration at 31 December 2016 was assessed at £3.8 million based on a projection of likely future capacity market clearing prices, discounted to present value at a risk free rate of 2%.

The provisional amounts recognised in respect of the identifiable assets acquired and liabilities assumed in the acquisition of the four companies, and measured at fair value, are set out in the table below:

	PPL £m	HPL £m	MPL £m	APL £m	Total £m
Financial assets	2.9	3.0	–	–	5.9
Property, plant and equipment	0.4	0.6	0.2	0.2	1.4
Financial liabilities	(2.9)	(3.0)	–	–	(5.9)
Intangible development asset	8.9	8.7	1.7	1.7	21.0
Total identifiable net assets	**9.3**	**9.3**	**1.9**	**1.9**	**22.4**
Goodwill	–	–	–	–	–
Fair value of consideration payable	**9.3**	**9.3**	**1.9**	**1.9**	**22.4**
Comprised of:					
Initial consideration payable on 3 January 2017 in cash	**7.4**	**7.4**	**1.9**	**1.9**	**18.6**
Fair value of contingent consideration	**1.9**	**1.9**	–	–	**3.8**

The intangible development assets identified as part of the acquisitions represent the value of planning and consent obtained for each site. No cash or cash equivalents were acquired in the transaction, therefore the net cash outflow on acquisition was £18.6 million.

The four acquired companies did not trade in the period between the acquisition date and the balance sheet, and no further costs were incurred. Accordingly, the Consolidated income statement includes no revenue or EBITDA in respect of the acquired companies. Transaction costs of £0.7 million were recognised as an expense in the period.

Acquisitions after the balance sheet date but before the financial statements were approved

The following disclosures relate to acquisitions completed between 1 January and 15 February 2017.

5.1 Acquisitions continued

Acquisition of Opus Energy Group Limited

On 6 December 2016, the Group announced the proposed acquisition of Opus Energy Group Limited (Opus Energy) for a consideration of £340 million, plus interest calculated on the amount of Opus Energy's net assets from 31 March 2016 to the acquisition completion date.

Opus Energy is a well-established energy retail business serving business customers in the SME market. The transaction represents a diversification of the Group's retail offering, strengthening our presence in the SME market, and provides a range of strategic and financial benefits. Opus Energy is expected to contribute positively to earnings and cash flow immediately following the acquisition and the combination provides a robust platform for future growth.

The transaction was approved by shareholders on 8 February 2017 and subsequently completed on 10 February 2017, the Group acquired 100% of the issued share capital on this date.

Total consideration paid in cash, including interest as described above, amounted to £367 million. No deferred or contingent consideration is payable. The acquisition was funded by a combination of existing cash reserves and a new £375 million loan facility which was partially drawn on 10 February 2017. Further details regarding the new facility are disclosed in note 4.3.

Given the short period of time between the transaction completion date and the approval of these financial statements, the initial accounting for the business combination is not complete. The table below provides the approximate acquisition date fair values of the assets acquired and liabilities assumed in the transaction based as the most recently available management information. These figures, including the indicative goodwill, are provisional.

	Total £m
Financial assets	169.9
Property, plant and equipment	5.6
Financial liabilities	(130.3)
Total identifiable net assets	**45.2**
Goodwill	322.1
Fair value of consideration payable	**367.3**

The provisional goodwill reflects the economic and strategic benefits described above. A full review and finalisation of identifiable intangible assets acquired will be completed before the initial accounting for the transaction is completed. Accordingly, the amount of goodwill recognised in the financial statements may be lower than indicated above.

The provisional financial assets acquired include £170 million of receivables, the majority of which reflect trade receivables for energy supplied to customers measured at cost. By virtue of their short tenor, the contractual amounts receivable and the fair value of these receivables are considered to be the same. A provision for doubtful debts of £3 million is included within the values above and reflects the best estimate of the contractual cash flows not expected to be recovered.

As the transaction completed after the balance sheet date, there are no amounts included in these financial statements in respect of the transaction other than transaction costs of £1.6 million incurred before 31 December 2016, which have been recognised as an expense in Operating and administrative costs in the income statement.

5.2 Goodwill and other intangible assets

Goodwill arises on the acquisition of a business when the consideration paid exceeds the fair value of the assets acquired. Our goodwill relates to the acquisition of Haven Power in 2009 and Billington Bioenergy in 2015. Other intangibles include development assets recognised on the acquisition of four OCGT development projects in 2016 and amounts paid in respect of carbon emission allowances for future years.

Accounting policy

Goodwill is initially recognised and measured at the acquisition date. Goodwill is not amortised but reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to the CGU to which it relates and the recoverable amount for that CGU assessed. Intangibles are recognised at fair value or cost.

The table shows movements and balances:

	Goodwill £m	Development assets £m	Carbon £m	Total £m
Cost and carrying amount:				
At 1 January 2015	10.7	–	–	10.7
Additions at cost	3.8	–	11.8	15.6
At 1 January 2016	14.5	–	11.8	26.3
Utilised in period	**–**	**–**	**(11.8)**	**(11.8)**
Additions at cost	**–**	**21.0**	**0.7**	**21.7**
At 31 December 2016	**14.5**	**21.0**	**0.7**	**36.2**

Goodwill

Total goodwill in the Consolidated balance sheet at 31 December 2016 and 31 December 2015 was £14.5 million, with £10.7 million arising on the acquisition of Haven Power in 2009 attributed to the Haven Power CGU and £3.8 million arising on the acquisition of Billington Bioenergy in 2015 attributable to the Billington Bioenergy CGU.

The recoverable amount of both the Haven Power and Billington Bioenergy CGUs is calculated annually, based on a value in use calculation. The approach for this calculation is the same as that used for the wider asset impairment review conducted by the Group as at 31 December 2016 and is disclosed in note 2.4. At 31 December 2016, the value in use of goodwill was significantly in excess of its book value in both the Haven Power and Billington Bioenergy CGUs.

Development assets

The development assets arose on the acquisition of four OCGT projects in December 2016 (see note 5.1) and reflect the value of planning and consents acquired as part of that transaction. They were measured at fair value on acquisition and will be amortised over the expected period of useful economic life of the projects once they reach commercial operations. Until operations commence, the assets are considered to have an indefinite life and thus will be subject to impairment testing at each balance sheet date.

At 31 December 2016, given the short time since the acquisition of the assets, management consider the fair value of the development assets to be equivalent to the purchase price.

Carbon assets

Carbon assets arise on the purchase of CO_2 emissions allowances in excess of the amount allocated under the ETS and required for the current financial year, and are measured at cost, net of any impairment.

The charge to the income statement, within fuel costs, reflects the cost of emissions allowances required to satisfy the obligation for the current year and takes into account generation and market purchases allocated to the current financial year, and to the extent further purchases are required, the market price at the balance sheet date.

5.3 Provisions

We make provision for reinstatement to cover the estimated costs of decommissioning and demolishing our generation assets and remediating the site at the end of the useful economic lives of the assets. The amount represents the discounted present value of the expected costs.

Accounting policy

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the 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 Group's generating assets, when a legal or constructive obligation arises, on a discounted basis. The amount provided represents the present value of the expected costs. In view of the uncertainty of assessing the amount of any proceeds from the disposal of the assets at the decommissioning date, no reduction in the provision is made for any such proceeds. The discount rate used is a risk free pre-tax rate of 1.9% (2015: 2.4%), reflecting the fact that the estimated future cash flows have built in risks specific to the liability. An amount equivalent to the discounted provision is capitalised within property, plant and equipment and is depreciated over the useful lives of the related assets. The unwinding of the discount is included in interest payable and similar charges.

	Reinstatement £m
Carrying amount:	
At 1 January 2015	29.8
Unwinding of discount	0.7
At 1 January 2016	30.5
Unwinding of discount	**0.8**
Adjustment for change in discount rate	**3.7**
At 31 December 2016	**35.0**

The provision is estimated using the assumption that the decommissioning and reinstatement will take place at the end of the expected useful life of the power station in 2039, and has been estimated using existing technology at current prices based on independent third party advice, updated on a triennial basis. The most recent update took place in December 2014.

SECTION 6:
OUR PEOPLE

The notes in this section relate to the remuneration of our directors and employees, including our obligations under retirement benefit schemes.

6.1 Employees and directors
This note provides a more detailed breakdown of the cost of our employees, including executive directors. The average number of employees in Operations (staff based at production sites), Retail services (employees in our Retail segment) and Central services (those working in central functions) are also provided.

Further information in relation to pay and remuneration of the executive directors can be found in the report of the Remuneration Committee, starting on page 82.

Staff costs (including executive directors)

	Years ended 31 December	
	2016 £m	2015 £m
Included in other operating and administrative expenses (note 2.3)		
Wages and salaries	74.3	79.8
Social security costs	8.1	9.4
Other pension costs	12.3	12.3
Share-based payments (note 6.2)	5.2	5.3
	99.9	106.8

Average monthly number of people employed (including executive directors)

	Years ended 31 December	
	2016 (number)	2015 (number)
Generation operations	645	644
Biomass supply operations	130	144
Retail services	399	353
Central services	293	301
	1,467	1,442

6.2 Share-based payments
We operate two share option schemes for our employees – the BMP for directors and senior executives, and the Savings-Related Share Option Plan (SAYE) for all qualifying employees. We incur a non-cash charge in respect of these schemes in our income statement, which is set out below along with a detailed description of each scheme and the number of options outstanding.

Accounting policy
All of the Group's share-based payments are equity-settled. Equity-settled share-based payments are measured at the fair value of the equity instrument at the date of grant and expensed on a straight-line basis over the relevant vesting period, based on an estimate of the shares that will ultimately vest as a result of the effect of non-market-based vesting conditions, which is revised at each balance sheet date.

Costs recognised in the income statement in relation to share-based payments during the year were as follows:

	Years ended 31 December	
	2016 £m	2015 £m
BMP	2.6	3.7
SAYE	2.6	1.6
	5.2	5.3

6.2 Share-based payments continued

Share Incentive Plan (SIP)

Between 2008 and 2010, qualifying employees could buy up to £1,500 worth of Partnership Shares in any one tax year. Matching shares were awarded to employees to match any shares they bought, in a ratio of one-to-one, with the cost of matching shares borne by the Group. There have been no awards under the SIP Partnership and Matching Share plan since 2010.

Shares in the Company held under trust and under the Company's control as a result of the SIP were as follows:

	Shares held at 1 January 2016 (number)	Shares acquired during year (number)	Shares transferred during year (number)	Shares held at 31 December 2016 (number)	**Cost at 31 December 2016 £000**	**Nominal value at 31 December 2016 £000**	**Market value at 31 December 2016 £000**
SIP	188,465	–	(35,431)	153,034	**1,436**	**18**	**578**

Bonus Matching Plan

Under the BMP, annual awards of performance and service-related shares are made for no consideration to executive directors and other senior executives up to a maximum of 150% of their annual bonus. A proportion of the shares vesting is conditional upon whether the Group's Total Shareholder Return (TSR) matches or outperforms an index (determined in accordance with the scheme rules) over three years and a proportion of the shares vesting is conditional upon performance against the internal balanced corporate scorecard. The fair value of the 2016, 2015 and 2014 BMP awards, of £2.6 million, £3.3 million and £5.4 million respectively, is being charged to the income statement on a straight-line basis over the corresponding three year vesting periods.

The fair value of BMP awards is calculated using a Monte-Carlo valuation model, which takes into account the estimated probability of different levels of vesting. The key inputs to the valuation model for the 2016 awards are the share price at the grant date (249.7 pence), expected volatility (41%), and risk free interest rate (0.45%). The fair value of each option granted was 153 pence.

Movements in the number of share options outstanding for the BMP awards is as follows:

	2016 BMP (number)	2015 BMP (number)
At 1 January	**3,411,792**	4,053,414
Granted	**1,686,095**	1,560,552
Forfeited	**(623,597)**	(505,781)
Exercised	**(337,146)**	(958,566)
Expired	**(943,212)**	(737,827)
At 31 December	**3,193,932**	3,411,792

50% of the BMP options granted in 2016 will vest conditional on Group TSR relative to the TSR of a comparator group of companies with the remaining 50% vesting conditional upon the internal balanced corporate scorecard (2015: 50% TSR-linked, 50% scorecard-linked). The share price on the grant date for BMP options awarded in the year was 250 pence (2015: 397 pence) and the weighted average fair value of the BMP options granted during the year was 153 pence (2015: 213 pence).

For the BMP options exercised during the period, the weighted average share price at the date of exercise was 232 pence (2015: 397 pence).

All of the BMP options outstanding at the end of the period had an exercise price of £nil (2015: £nil). The weighted average remaining contractual life was 17 months (2015: 14 months).

The number of options exercisable at the year end was nil (2015: nil).

6.2 Share-based payments continued

Savings-Related Share Option Plan (SAYE)

In April 2016, participation in the SAYE Plan was offered again to all qualifying employees. Options were granted for employees to acquire shares at a price of 203 pence (2015: 319 pence), representing a discount of 20% to the prevailing market price determined in accordance with the scheme rules. The options are exercisable at the end of three or five year savings contracts. The fair value of the options granted in connection with the SAYE Plan of £3.9 million (2015: £4.4 million) is being charged to the income statement over the term of the relevant contracts.

Movements in the number of share options outstanding for the SAYE plans are as follows:

	2016		2015	
	SAYE three-year (number)	SAYE five-year (number)	SAYE three-year (number)	SAYE five-year (number)
At 1 January	1,948,209	934,041	963,911	1,107,420
Granted	3,150,023	919,723	2,127,867	862,670
Forfeited	(73,907)	–	(16,683)	(5,440)
Exercised	(8,618)	(8,604)	(2,414)	(437,976)
Expired	(1,728,801)	(848,451)	(1,124,472)	(592,633)
At 31 December	3,286,906	996,709	1,948,209	934,041

The fair value of SAYE awards is calculated using a Black-Scholes model, which compares exercise price to share price at the date of grant.

The fair value of SAYE options granted and the inputs to the option pricing model used in the current and previous year are set out in the table below:

Grant date	5 April 2016	5 April 2016	2 April 2015	2 April 2015
Share price at grant date (pence)	286	286	399	399
Vesting period	3 years	5 years	3 years	5 years
Exercise price (pence)	203	203	319	319
Dividend yield	2.9%	5.0%	1.9%	1.9%
Annual risk free interest rate	0.81%	0.95%	1.08%	1.36%
Expected volatility	40.0%	37.6%	43.0%	43.0%
Fair value of options granted (pence)	101	82	142	160

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous three and five years respectively. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

For the SAYE options exercised during the period, the weighted average share price at the date of exercise was 337 pence (2015: 400 pence).

The weighted average exercise price of SAYE options outstanding at the end of the period was 216 pence (2015: 331 pence). The weighted average remaining contractual life was 31 months (2015: 32 months).

The number of options exercisable at the year end was nil (2015: 10,894).

Additional information in relation to the Group's share-based incentive plans is included in the Remuneration Committee report.

6.3 Retirement benefit obligations

We operate a defined benefit and three defined contribution pension schemes.

The Drax Power Group (DPG) section of the Electricity Supply Pension Scheme (ESPS) is a defined benefit scheme; a pension arrangement under which participating members receive a pension benefit at retirement determined by the scheme rules. Members are typically entitled to an annual pension on retirement of 1/80th of final pensionable salary for each year of service plus a tax-free lump sum of three times pension.

The Drax Group Personal Pension Plan, Haven Power Personal Pension Plan and Drax Biomass Inc. 401(K) Plan are defined contribution schemes, which provide a retirement benefit that is dependent upon actual contributions made by the Group and members of the relevant scheme.

6.3 Retirement benefit obligations continued

Accounting policy

Payments to defined contribution schemes are recognised as an expense when employees have rendered services that entitle them to the contributions.

For the defined benefit pension scheme, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out at the end of each reporting period. Remeasurement of the obligation, comprising actuarial gains and losses, the effect of the asset ceiling (if applicable) and the return on scheme assets (excluding interest), is recognised immediately in the balance sheet with a charge or credit to the statement of comprehensive income in the period in which it occurs. Defined benefit costs, including current service costs, past service costs and gains and losses on curtailments and settlements are recognised in the income statement as part of operating and administrative expenses in the period in which they occur. The net interest expense is recognised in finance costs.

The income statement charge for the defined contribution scheme represents the contributions due to be paid by the Group in respect of the current period.

Significant judgement areas

Measurement of the defined benefit obligation using the projected unit credit method involves the use of key assumptions, including discount rates, inflation rates, salary and pension increases, and mortality rates. These actuarial assumptions are reviewed annually and modified as appropriate. The Group believes that the assumptions utilised in measuring obligations under the scheme are reasonable based on prior experience, market conditions and the advice of scheme actuaries. However, actual results may differ from such assumptions.

The assumptions applied in 2016 have been prepared on a consistent basis with those in the previous period and in accordance with independent actuarial advice received.

Defined contribution schemes

The Group operates three defined contribution schemes, The Drax Group Personal Pension Plan, Haven Power Personal Pension Plan and Drax Biomass inc. 401(K) Plan, for all qualifying employees. Pension costs for the defined contribution schemes are as follows:

	Years ended 31 December	
	2016 £m	2015 £m
Total included in staff costs (note 6.1)	**5.6**	5.9

As at 31 December 2016, contributions of £0.5 million (2015: £0.4 million) due in respect of the current reporting period had not been paid over to the schemes. The Group has no further payment obligations once the contributions have been paid.

Defined benefit scheme

The DPG section of the ESPS was closed to new members as from 1 January 2002 unless they qualify through being existing members of another part of the ESPS. Members who joined before this date continue to build up pension benefits as part of the scheme.

The DPG ESPS exposes the Group to actuarial and other risks, the most significant of which are considered to be:

Investment risk	The scheme liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The scheme holds a significant proportion of growth assets (equities, property and direct lending) which, though expected to outperform corporate bonds in the long term, create volatility and risk in the short term. The allocation to growth assets is monitored to ensure it remains appropriate given the scheme's long term objectives.
Discount rate risk	A decrease in corporate bond yields will increase the value placed upon the scheme's liabilities, although this will be partially offset by an increase in the value of the scheme's bond holdings.
Longevity risk	The majority of the scheme's obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities of the scheme.
Inflation risk	The majority of the scheme's obligations to pay benefits are linked to inflation, and as such higher inflation will lead to higher liabilities. The majority of the assets held by the scheme are either unaffected by or only loosely correlated with inflation, such that an increase in inflation will also increase the deficit. In most cases, caps on inflationary increases are in place, to protect against extreme inflation.

6.3 Retirement benefit obligations continued

Other risks include operational risks (such as paying out the wrong benefits), legislative risks (such as the Government increasing the burden on pension schemes through new legislation) and other demographic risks (such as making a higher proportion of members with dependants eligible to receive pensions from the Group). The Trustees insure certain benefits payable on death before retirement.

A contingent liability exists in relation to the equalisation of Guaranteed Minimum Pension. See note 7.5 for details.

The most recent funding valuation of the DPG ESPS carried out by Aon Hewitt, a qualified independent actuary, as at 31 March 2016 is not yet complete; however the actuarial review at 31 December 2016 is based on the same membership and other data as the initial results of this funding valuation. The scheme board accepted the advice of the actuary and approved the use of these assumptions for the purpose of assessing the scheme cost. Future valuations are required by law at intervals of no more than three years.

The results of the latest funding valuation at 31 March 2016 have been adjusted to the balance sheet date, taking into account experience over the period since 31 March 2016, changes in market conditions and differences in financial and demographic assumptions. The present value of the defined benefit obligation, and the related current service cost were measured using the projected unit credit method. The principal assumptions used, which reflect the nature and term of the scheme liabilities, are as follows:

	As at 31 December	
	2016 % p.a.	2015 % p.a.
Discount rate	**2.8**	3.9
Inflation (RPI)	**3.2**	3.1
Rate of increase in pensions in payment and deferred pensions	**3.1**	3.0
Rate of increase in pensionable salaries	**3.8**	3.7

Mortality assumptions are based on recent actual mortality experience of scheme members and allow for expected future improvements in mortality rates. The assumptions are that a member aged 60 in 2016 will live, on average, for a further 27 years if they are male (2015: 27 years) and for a further 29 years if they are female (2015: 29 years). Life expectancy at age 60 for male and female non-pensioners currently aged 45 is assumed to be 28 and 31 years respectively (2015: 28 and 31 years respectively).

The net liability recognised in the balance sheet is the excess of the present value of the defined benefit obligation over the fair value of the plan assets, determined as follows:

	As at 31 December	
	2016 £m	2015 £m
Defined benefit obligation	**311.4**	244.6
Fair value of plan assets	**(281.3)**	(215.1)
Net liability recognised in the balance sheet	**30.1**	29.5

The amounts recognised in the income statement, within other operating and administrative expenses and finance costs, are as follows:

	Years ended 31 December	
	2016 £m	2015 £m
Included in staff costs (note 6.1):		
Current service cost	**6.0**	6.4
Included in finance costs (note 2.5):		
Interest on net defined benefit liability	**0.9**	1.1
Total amounts recognised in the income statement	**6.9**	7.5

Actuarial gains and losses are recognised in the statement of comprehensive income in full, as follows:

	Years ended 31 December	
	2016 £m	2015 £m
Cumulative actuarial losses on defined benefit pension scheme at 1 January	**(70.8)**	(72.0)
Actuarial (losses)/gains on defined benefit pension scheme recognised in the year	**(8.4)**	1.2
Cumulative losses recognised in the statement of comprehensive income at 31 December	**(79.2)**	(70.8)

6.3 Retirement benefit obligations continued

Changes in the present value of the defined benefit obligation are as follows:

	Years ended 31 December 2016 £m	2015 £m
Defined benefit obligation at 1 January	**244.6**	242.1
Current and past service cost	**6.0**	6.4
Employee contributions	**0.2**	0.2
Interest cost	**9.4**	8.9
Actuarial (gains)/losses	**58.8**	(5.8)
Benefits paid	**(7.6)**	(7.2)
Defined benefit obligation at 31 December	**311.4**	244.6

The actuarial losses of £58.8 million (2015: £5.8 million gains) reflect losses of £71.4 million arising from changes in financial assumptions (2015: gains of £2.3 million), offset by £1.9 million gains arising from changes in demographic assumptions and gains arising from scheme experience of £10.7 million (2015: gains of £1.8 million and £1.7 million respectively).

The losses due to changes in financial assumptions principally reflect the increase in the present value of the scheme liabilities arising as a result of the change in discount rate assumption to 2.75% (2015: 3.9%) following reductions in corporate bond yields.

Changes in the fair value of plan assets are as follows:

	Years ended 31 December 2016 £m	2015 £m
Fair value of plan assets at 1 January	**215.1**	207.8
Interest income on plan assets	**8.5**	7.8
Remeasurement (losses)/gains	**50.4**	(4.6)
Employer contributions	**14.7**	11.1
Employee contributions	**0.2**	0.2
Benefits paid	**(7.6)**	(7.2)
Fair value of plan assets at 31 December	**281.3**	215.1

Employer contributions included payments totalling £8.3 million (2015: £5.1 million) to reduce the actuarial deficit.

The actual return on plan assets in the period was £58.9 million (2015: £3.2 million).

The fair values of the major categories of plan assets were as follows:

	As at 31 December 2016 £m	2015 £m
Gilts	**105.9**	–
Equities(1)	**65.2**	64.6
Fixed interest bonds(2)	**61.3**	113.9
Property	**29.5**	27.9
Cash and other assets(3)	**19.4**	8.7
Fair value of total plan assets	**281.3**	215.1

Notes:
(1) At 31 December 2016 the scheme's long-term asset strategy was: global equity (20%), direct lending (10%), emerging market equity (5%), fixed interest bonds (15%), corporate bonds (6%), liability driven investing (29%) and long lease property (15%).
(2) Fixed interest bonds include a mixture of corporate, Government and absolute return bonds. Approximately 27% of the bonds have a sub-investment grade credit rating (i.e. BB+ or lower).
(3) Other assets include £19.1 million of investments in direct lending, a type of private equity vehicle, which is not quoted in an active market (2015: £7.9 million).

6.3 Retirement benefit obligations continued

The pension plan assets do not include any ordinary shares issued by Drax Group plc or any property occupied by the Group.

The Group employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class relative to the actual asset allocation for the scheme.

The assumptions for discount rate, inflation rate, rate of increase in pensions paid and expected return on plan assets all have a potentially significant effect on the measurement of the scheme deficit. The following table provides an indication of the sensitivity of the pension deficit at 31 December 2016 to changes in these assumptions:

		%	(Decrease)/ Increase in net liability £m
Discount rate	– Increase	0.25	(15.6)
	– Decrease	0.25	16.2
Inflation rate[1]	– Increase	0.25	(14.0)
	– Decrease	0.25	13.6
Life expectancy	– Increase	1 year	(10.9)
	– Decrease	1 year	11.0

Note:
(1) The sensitivity of the scheme liabilities to salary and pension increases is closely correlated with inflation.

The Group is exposed to investment and other experience risks, as described above, and may need to make additional contributions where it is estimated that the benefits will not be met from regular contributions and expected investment income.

	As at 31 December				
	2016 £m	2015 £m	2014 £m	2013 £m	2012 £m
Defined benefit obligation	**(311.4)**	(244.6)	(242.1)	(220.9)	(199.0)
Fair value of plan assets	**281.3**	215.1	207.8	179.2	156.9
Deficit	**(30.1)**	(29.5)	(34.3)	(41.7)	(42.1)
Experience adjustments on plan liabilities	**10.7**	1.7	1.6	8.7	(1.7)
Experience adjustments on plan assets	**50.4**	(4.6)	13.6	9.4	(3.0)

The defined benefit obligation includes benefits for current employees of the Group (60%), former employees of the Group who are yet to retire (5%) and retired pensioners (35%). The weighted-average period over which benefit payments are expected to be made, or the duration of the scheme liabilities, was assessed at the 31 March 2016 funding valuation to be 21 years.

The Group expects to contribute £23.8 million to the defined benefit pension plan during the 12 months ended 31 December 2017 and make regular deficit contributions over the period to 2025.

The Group intends to fund the deficit, agreed at the 31 March 2013 funding valuation, over the period to 31 December 2019.

SECTION 7:

RISK MANAGEMENT

This section provides disclosures around financial risk management, including the financial instruments we use to mitigate such risks.

7.1 Financial risk management

The Group's activities expose it to a variety of financial risks including commodity price risk, interest rate risk, foreign currency risk, liquidity risk, counterparty risk and credit risk. The Group's overall risk management programme focuses on the unpredictability of commodity and financial markets and seeks to manage potential adverse effects on the Group's financial performance.

The Group uses derivative financial instruments to hedge certain risk exposures. Risk management is carried out by the risk management committees as explained in Principal risks and uncertainties (page 55) which identify, evaluate and hedge financial risks in close coordination with the Group's trading function under policies approved by the Board of directors.

Commodity price risk

The Group is exposed to the effect of fluctuations in commodity prices, particularly the price of electricity, the price of coal, sustainable wood fibre and pellets and other fuels, and the price of CO_2 emissions allowances. Price variations and market cycles have historically influenced the financial results of the Group and are expected to continue to do so.

The Group has a policy of securing forward power sales, purchases of fuel and CO_2 emissions allowances when profitable to do so. All commitments to sell power under fixed price contracts are designated as cash flow hedges as they reduce the Group's cash flow exposure resulting from fluctuations in the price of electricity.

The Group purchases coal, sustainable biomass and other fuels under either fixed or variable priced contracts with different maturities from a variety of domestic and international sources. All international physical coal purchase contracts transacted at a fixed price and financial coal contracts exchanging floating price coal for fixed price amounts are designated as cash flow hedges as they reduce the Group's cash flow exposure resulting from fluctuations in the price of coal.

The Group purchases CO_2 emissions allowances under fixed price contracts with different maturity dates from a range of domestic and international sources. All commitments to purchase CO_2 emissions allowances under fixed price contracts are designated as cash flow hedges as they reduce the Group's cash flow exposure resulting from fluctuations in the price of CO_2 emissions allowances.

Commodity price sensitivity

The sensitivity analysis below has been determined based on the exposure to commodity prices for outstanding monetary items at the balance sheet date. The analysis is based on the Group's commodity financial instruments held at each balance sheet date.

If commodity prices had been 5% higher/lower and all other variables were held constant, the Group's:

- profit after tax for the year ended 31 December 2016 would increase/decrease by £3.4 million (2015: decrease/increase by £6.7 million). This is mainly attributable to the Group's exposure to oil derivatives; and
- the hedge reserve would increase/decrease by £36.3 million (2015: decrease/increase by £11.5 million) mainly as a result of the changes in the fair value of financial coal and power derivatives.

Interest rate risk

Historically the Group has been exposed to interest rate risk principally in relation to its bank debt, and has sought to mitigate this risk with interest rate hedges on a proportion of its debt facilities. The Group has no interest rate swaps outstanding at the balance sheet date; however this risk management tool remains available to the Group. Information about the Group's instruments that are exposed to interest rate risk and their repayment schedules is provided below.

Interest rate sensitivity

The sensitivity analysis below has been determined based on the exposure to interest rates for non-derivative instruments at the balance sheet date. For floating rate liabilities, the analysis is prepared assuming the amount of the liability outstanding at the balance sheet date was outstanding for the whole year.

If interest rates had been 1% higher/lower and all other variables were held constant, the Group's profit after tax and net assets for the year ended 31 December 2016 would decrease/increase by £1.8 million (2015: decrease/increase by £1.8 million) as a result of the changes in interest payable during the period.

7.1 Financial risk management continued

Foreign currency risk

Forward foreign currency exchange contracts are entered into in order to hedge fixed price international coal purchases in US dollars, wood pellet purchases in US dollars, Canadian dollars and Euros, and CO_2 emissions allowances purchases in Euros.

Exchange rate exposures are managed within approved policy parameters utilising a variety of foreign currency exchange contracts. The Group enters into forward currency purchase contracts to hedge its anticipated foreign currency requirements over a rolling five-year period for both contracted and forecast transactions.

Foreign currency sensitivity

If sterling exchange rates had been 5% stronger/weaker against other currencies and all other variables were held constant, the Group's:

– profit after tax for the year ended 31 December 2016 would decrease/increase by £252.6 million/£277.7 million (2015: decrease/increase by £233.0 million/£241.1 million). This is mainly attributable to the Group's exposure to foreign currency exchange contracts entered in relation to fuel purchase contracts; and
– other equity reserves would increase/decrease by £78.7 million/£87 million (2015: increase/decrease by £67.8 million/£75.0 million) as a result of the changes in the fair value of foreign currency exchange contracts.

Liquidity risk

The treasury function is responsible for liquidity, funding and settlement management under policies approved by the Board of directors. Liquidity needs are monitored using regular forecasting of operational cash flows and financing commitments. The Group maintains a mixture of cash and cash equivalents, and committed facilities in order to ensure sufficient funding for business requirements.

The following tables set out details of the expected contractual maturity of non-derivative financial liabilities. The tables include both interest and principal cash flows. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate curves at the balance sheet date.

	As at 31 December 2016			
	Within 3 months £m	3 months– 1 year £m	>1 year £m	Total £m
Term loans, gross value	**3.0**	**46.7**	**326.7**	**376.4**
Finance lease liabilities, carrying value	**0.1**	**0.1**	**1.0**	**1.2**
Borrowings, contractual maturity	**3.1**	**46.8**	**327.7**	**377.6**
Trade and other payables	**400.1**	**181.7**	**10.1**	**591.9**
	403.2	**228.5**	**337.8**	**969.5**

	As at 31 December 2015			
	Within 3 months £m	3 months– 1 year £m	>1 year £m	Total £m
Term loans, gross value	3.1	9.8	374.5	387.4
Finance lease liabilities, carrying value	–	0.3	0.6	0.9
Borrowings, contractual maturity	3.1	10.1	375.1	388.3
Trade and other payables	327.2	147.7	13.1	488.0
	330.3	157.8	388.2	876.3

Interest payments are calculated based on forward interest rates estimated at the balance sheet date using publicly available information.

The weighted average interest rate payable at the balance sheet date on our term loans was 4.17% (2015: 4.22%).

7.1 Financial risk management continued

The following tables set out details of the expected contractual maturity of derivative financial instruments which are marked to market, based on the undiscounted net cash inflows/(outflows). Where the amount payable or receivable is not fixed, the amount disclosed has been determined by reference to projected commodity prices, or foreign currency exchange rates, as illustrated by the yield or other forward curves existing at the reporting date.

	As at 31 December 2016			
	Within 1 year £m	1–2 years £m	>2 years £m	Total £m
Commodity contracts, net	**78.7**	**(25.1)**	**(14.2)**	**39.4**
Forward foreign currency exchange contracts, net	**903.5**	**870.9**	**1,696.5**	**3,470.9**
	982.2	**845.8**	**1,682.3**	**3,510.3**

	As at 31 December 2015			
	Within 1 year £m	1–2 years £m	>2 years £m	Total £m
Commodity contracts, net	233.1	(84.5)	(73.0)	75.6
Forward foreign currency exchange contracts, net	1,019.1	1,005.5	1,859.2	3,883.8
	1,252.2	921.0	1,786.2	3,959.4

In managing liquidity risk, the Group has access to facilities that enable it to accelerate the cash flows associated with certain of its receivables (principally those related to ROC sales and retail power sales). Each of these facilities is provided on a non-recourse basis and accordingly receivables sold under each facility are derecognised from the balance sheet at the point of sale. At the balance sheet date there was £111.1 million utilised under ROC agreements and £74.4 million utilised under Receivable financing agreements.

Counterparty risk

As the Group relies on third party suppliers for the delivery of currency, coal, sustainable compressed wood pellets and other goods and services, it is exposed to the risk of non-performance by these third party suppliers. If a large supplier were to fall into financial difficulty and/or fail to deliver against its contract with the Group, there would be additional costs associated with securing the lost goods or services from other suppliers.

The Group enters into contracts for the sale of electricity to a number of counterparties. The failure of one or more of these counterparties to perform their contractual obligations may cause the Group financial distress or increase the risk profile of the Group.

Credit risk

The Group's exposure to credit risk is limited to the carrying amount of financial assets recognised at the balance sheet date, as summarised below:

	As at 31 December	
	2016 £m	2015 £m
Financial assets:		
Cash and cash equivalents	**228.4**	133.8
Trade and other receivables	**296.9**	324.2
Derivative financial instruments	**891.3**	609.2
	1,416.6	1,067.2

Trade and other receivables are stated gross of the provision for doubtful debts of £4.0 million (2015: £4.9 million).

Credit exposure is controlled by counterparty limits that are reviewed and approved by risk management committees. Where considered appropriate, counterparties are required to provide credit support in the form of a parent company guarantee, letter of credit, deed of charge, or cash collateral. In addition, where deemed appropriate the Group has historically purchased credit default swaps.

The investment of surplus cash is undertaken to maximise the return within Board approved policies. These policies manage credit risk exposure by setting out minimum rating requirements, maximum investment with any one counterparty and the maturity profile.

7.1 Financial risk management continued

Capital management

The Group manages its capital to ensure it is able to continue as a going concern, and maintain its credit rating while maximising the return to shareholders through the optimisation of the debt and equity balance. The capital structure of the Group consists of shareholders' equity (excluding the hedge reserve), plus net debt. Net debt is comprised of borrowings disclosed in note 4.3 and cash and cash equivalents in note 4.2.

	As at 31 December	
	2016 £m	2015 £m
Borrowings	**321.9**	320.4
Cash and cash equivalents	**(228.4)**	(133.8)
Net debt	**93.5**	186.6
Total shareholders' equity, excluding hedge reserve	**1,739.8**	1,567.5

Dividend policy

It is the Group's policy to distribute 50% of underlying profit after tax to shareholders each year. The policy is designed to ensure dividends reflect the underlying trading performance of the business whilst retaining sufficient cash within the Group to support strategic development objectives and working capital requirements. Underlying earnings are based on earnings calculated in accordance with IFRS adjusted to exclude the post-tax impact of unrealised gains and losses on derivative contracts and any other one-off or otherwise exceptional items that the Board considers to be unrepresentative of the Group's trading and operational performance.

7.2 Derivative financial instruments

We enter into forward contracts for the purchase and sale of physical commodities (principally power, gas, coal, sustainable biomass and CO_2 emissions allowances) to secure market level bark and dark green spreads on future electricity sales, and also financial contracts (principally currency exchange contracts and financial coal and oil derivatives) to fix Sterling cash flows.

We hold these contracts for risk management purposes, to manage key risks facing the business including commodity price risk and foreign currency risk (see note 7.1).

A successful commercial hedging strategy is critical to our business model. Our policy is to fix exposures to commodity price movements and changes in foreign exchange rates using derivative contracts such as those described above. This strategy aims to de-risk the business, providing security and certainty over cash flows into the future. As at 31 December 2016, due to the weakening of Sterling against the US dollar, our forward derivative contracts, consisting largely of forward contracts for the purchase of foreign currencies (principally for the purpose of fixing the Sterling cost of sustainable compressed wood pellet purchases), increased to £545.1 million (2015: £143 million) thereby protecting the Group to that extent from the increased cost of future supplies denominated in foreign currencies from the weakness of Sterling.

Accounting policy

At the balance sheet date all contracts (subject to certain exemptions described below) must be measured at fair value, which is in essence the difference between the price we have secured in the contract, and the price we could achieve in the market at that point in time.

Changes in fair value are recognised either within the income statement or the hedge reserve, dependent upon whether the contract in question qualifies as an effective hedge under IFRS (see note 7.4).

Where possible, the Group has taken advantage of the own use exemption which allows qualifying contracts to be excluded from fair value mark-to-market accounting. This applies to certain contracts for physical commodities entered into and held for our own purchase, sale or usage requirements, including forward contracts for the purchase of biomass, and coal from domestic sources.

Contracts which do not qualify for the own use exemption – principally power, gas, financial oil, financial coal, CO_2 emissions allowances and forward foreign currency exchange contracts – are accounted for as derivatives in accordance with IAS 39 and are recorded in the balance sheet at fair value, with changes in fair value reflected through the hedge reserve (note 7.4) to the extent that the contracts are designated as effective hedges in accordance with IAS 39, or the income statement where the hedge accounting requirements are not met. The Group enters into forward contracts solely for the purpose of financial risk management and considers all of its contracts to be economic hedges, regardless of whether the specific criteria for hedge accounting are met.

Derivative financial instruments with a maturity date within 12 months from the balance sheet date are classified as current assets or liabilities. Instruments with a maturity date beyond 12 months are classified as non-current assets or liabilities.

7.2 Derivative financial instruments continued

The location in the consolidated financial statements of the changes in fair value of derivative contracts in 2016 is summarised in the table below:

Accounting for derivative contracts	Gains/(losses) on contracts in 2016	Accounting treatment for gains/(losses) in the consolidated financial statements
Commodity contracts		
Power	(88.6)	Hedge reserve
Coal from international sources	5.6	Income statement
Coal from domestic sources	n/a	Own-use exemption
Biomass	n/a	Own-use exemption
CO_2 emissions allowances	(2.7)	Hedge reserve
Gas	(76.5)	Income statement
Financial contracts		
Foreign currency exchange contracts	241.9	Income statement
	384.1	Hedge reserve
Financial coal	(13.7)	Income statement
	37.3	Hedge reserve
Financial oil and other financial products	19.5	Income statement
Total net gains in hedge reserve	330.1	
Total net gains in income statement	176.8	

Critical judgement areas

The fair values of derivative instruments for commodities and foreign currency exchange contracts are determined using forward price curves. Forward price curves represent the Group's estimates of the prices at which a buyer or seller could contract today for delivery or settlement of a commodity or foreign exchange payment or receipt, at future dates. The Group generally bases forward price curves upon readily obtainable market price quotations, as the Group's commodity and forward foreign exchange contracts do not generally extend beyond the actively traded portion of these curves. However, the forward price curves used are only an estimate of how future prices will move and are, therefore, subjective. Where derivative financial instruments include options these are valued using an option pricing model. Inputs to the model include market commodity prices, forward price curves, the term of the option, discount rate and assumptions around volatility based on historical movements. The inputs include assumptions around future transactions and market movements, as well as credit risk and are, therefore, subjective.

Fair value accounting

Forward contracts for the sale of power, purchase of coal from international sources, purchase of CO_2 emissions allowances, financial coal, financial oil, gas (collectively "Commodity contracts") and foreign currency exchange contracts are recorded in the balance sheet at fair value as follows:

	As at 31 December 2016		As at 31 December 2015	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Commodity contracts:				
Less than one year	**91.1**	**(164.0)**	264.1	(226.1)
More than one year but not more than two years	**9.8**	**(51.7)**	81.2	(94.1)
More than two years	**1.9**	**(7.5)**	27.0	(53.4)
Forward foreign currency exchange contracts:				
Less than one year	**313.9**	**(87.0)**	66.7	(48.2)
More than one year but not more than two years	**185.8**	**(26.0)**	93.8	(81.7)
More than two years	**288.8**	**(27.3)**	76.4	(70.9)
Total	**891.3**	**(363.5)**	609.2	(574.4)
Less: non-current portion				
Commodity contracts	**(11.7)**	**59.2**	(108.2)	147.5
Forward foreign currency exchange contracts	**(474.6)**	**53.3**	(170.2)	152.6
Total non-current portion	**(486.3)**	**112.5**	(278.4)	300.1
Current portion	**405.0**	**(251.0)**	330.8	(274.3)

7.2 Derivative financial instruments continued

The total movement in the fair value of these contracts of £506.9 million (2015: £147.1 million gain) is recognised in the income statement or the hedge reserve, dependent upon whether the hedge accounting requirements of IAS 39 are met, as follows:

	Years ended 31 December 2016 £m	2015 £m
Unrealised gains on derivative contracts recognised in arriving at operating profit	**176.8**	123.7
Unrealised gains on derivative contracts recognised in the hedge reserve (note 7.4)	**330.1**	23.4
Total unrealised gains on derivative contracts	**506.9**	147.1

We maintain a substantial foreign currency hedging programme to secure the sterling cost of future purchases of fuel in foreign currencies. The vast majority of our fuel purchases, and therefore our currency exchange contracts, are denominated in US dollars. Compared to market exchange rates immediately prior to the EU referendum in June 2016, Sterling depreciated by approximately 15–20% against the US dollar by the balance sheet date. As a result, combined with the high volume of such contracts held (shown in the table on page 161), the net unrealised gains recognised in the year principally reflect the value of our forward currency purchase contract portfolio.

A material proportion of these contracts are not designated in hedge accounting relationships under IAS 39 and thus the gains on these contracts were recognised in the income statement.

Unrealised gains recognised in the hedge reserve principally reflect gains on the portion of our forward currency exchange contracts that are designated in effective hedge relationships in accordance with IAS 39.

Fair value measurement

- **Commodity contracts fair value –** The fair value of open commodity contracts that do not qualify for the own use exemption is calculated by reference to forward market prices at the balance sheet date. As contracts are generally short-term, forward market price curves are available for the duration of the contracts. The quoted market price used for financial assets held by the Group is the current bid price; the quoted price for financial liabilities is the current ask price.
- **Forward foreign currency exchange contracts fair value –** The fair value of forward foreign currency exchange contracts is determined using forward currency exchange market rates at the balance sheet date.
- **Other financial contracts fair value –** The fair value of other financial contracts that do not qualify for the own use exemption, is calculated by reference to forward market prices at the balance sheet date. As contracts are generally short-term, forward market price curves are available for the duration of the contracts.

The fair values of all derivative financial instruments are discounted to reflect the credit risk inherent within the instrument.

The Group has reviewed all significant contracts for the presence of embedded derivatives. Where contracts were found to contain embedded derivatives, they were considered to be closely related to the economic characteristics and risks of the host contract, and therefore do not require separate valuation from their host contracts.

We are required by IFRS to categorise our financial instruments in accordance with the following hierarchy in order to explain the basis on which their fair values have been determined:

Level 1 – fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
Level 2 – fair value measurements are those derived from inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
Level 3 – fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Categorisation within this fair value measurement hierarchy has been determined on the basis of the lowest level input that is significant to the fair value measurement of the relevant asset or liability.

The fair value of commodity contracts, forward foreign currency exchange contracts and the contingent consideration in the OCGT acquisition (see note 5.1) are largely determined by comparison between forward market prices and the contract price; therefore these contracts are categorised as Level 2.

There have been no transfers during the year between Level 1, 2 or 3 category inputs.

7.3 Other financial instruments

We hold a variety of other non-derivative financial instruments, including cash and cash equivalents, borrowings, payables and receivables arising from our operations.

Accounting policy

Cash and cash equivalents (note 4.2), trade and other receivables (note 3.4), and trade and other payables (note 3.5) generally have short times to maturity. For this reason their carrying values, on the historical cost basis, approximate to their fair value. The Group's borrowings (note 4.3) relate principally to amounts drawn down against term loans, the carrying amounts of which approximate their fair values by virtue of being floating rate instruments.

7.4 Hedge reserve

Changes in the fair value of our derivative commodity, financial and currency contracts are recognised in the hedge reserve, to the extent that they qualify as effective hedges under accounting rules. The cumulative gains and losses unwind and are released as the related contracts mature and we take delivery of the associated commodity or currency.

As described in note 7.2, all of our derivative contracts are entered into for the purpose of commercial hedging; however, not all of these contracts qualify as effective hedges under IAS 39. The changes in fair value of contracts that do not meet the definition of an IFRS effective hedge are recognised in the income statement. Managing our principal risks and uncertainties is about locking down exposures to moving prices and securing market level dark green and bark spreads for the future.

The Group designates certain hedging instruments used to address commodity price risk and foreign exchange risk as cash flow hedges. At the inception of the hedge, the relationship between the hedging instrument and hedged item is documented, along with its risk management objectives. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instruments used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items. Changes in fair value of contracts designated into such hedging relationships are recognised within the hedge reserve to the extent they are effective.

	Years ended 31 December	
	2016 £m	2015 £m
At 1 January	**34.9**	16.4
Gains/(losses) recognised:		
– Commodity contracts	**(18.3)**	41.4
– Forward foreign currency exchange contracts	**397.3**	27.7
Released from equity:		
– Commodity contracts	**(35.7)**	(49.2)
– Forward foreign currency exchange contracts	**(13.2)**	3.5
Related deferred tax, net (note 2.6)	**(59.6)**	(4.9)
At 31 December	**305.4**	34.9

The Group's cash flow hedges relate to commodity contracts (principally commitments to sell power) and forward foreign currency exchange contracts. Amounts are recognised in the hedge reserve as the designated contracts are marked to market at each period end for the effective portion of the hedge, which is generally 100% of the relevant contract. Amounts held within the hedge reserve are then released as the related contract matures and the hedged transaction impacts profit or loss. For power sales contracts, this is when the underlying power is delivered. For currency contracts, this is when the associated foreign currency transaction is recognised. Further information about the Group's accounting for financial instruments is included in note 7.2.

The expected release profile from equity of post-tax hedging gains and losses is as follows:

	As at 31 December 2016			
	Within 1 year £m	**1–2 years £m**	**>2 years £m**	**Total £m**
Commodity contracts	**(12.8)**	**(0.6)**	**0.1**	**(13.3)**
Forward foreign currency exchange contracts	**42.8**	**69.0**	**206.9**	**318.7**
	30.0	**68.4**	**207.0**	**305.4**

	As at 31 December 2015			
	Within 1 year £m	1–2 years £m	>2 years £m	Total £m
Commodity contracts	27.9	4.8	(0.8)	31.9
Forward foreign currency exchange contracts	7.8	(10.0)	5.2	3.0
	35.7	(5.2)	4.4	34.9

7.5 Contingent liabilities

Contingent liabilities are potential future outflows of cash that are dependent on a future event that is outside of our control. The amount and timing of any payment is uncertain, cannot be measured reliably, or is considered to be unlikely.

Guaranteed Minimum Pension (GMP)

The UK Government intends to implement legislation to equalise the GMP, resulting in an increase in the value of GMP for males. This would correspondingly increase the defined benefit pension obligation of the Group (note 6.3). At present, the methodology for implementing the equalisation is uncertain and thus the impact cannot be reliably measured. As a result, no allowance has been made for GMP equalisation in the calculation of the defined benefit obligation within these consolidated financial statements.

Borrowings

In addition to the amount drawn down against the bank loans, certain members of the Group guarantee the obligations of a number of banks in respect of letters of credit issued by those banks to counterparties of the Group. As at 31 December 2016 the Group's contingent liability in respect of letters of credit issued under the revolving credit facility amounted to £57.9 million (2015: £37.9 million).

7.6 Commitments

We have a number of financial commitments (i.e. a contractual requirement to make a cash payment in the future) that are not recorded in our balance sheet as the contract is not yet due for delivery. Such commitments include contracts for the future purchase of coal and biomass, operating leases for land and buildings, contracts for the construction of assets and contracts for the provision of services.

	As at 31 December	
	2016 £m	2015 £m
Contracts placed for future capital expenditure not provided in the financial statements	**33.0**	43.2
Future support contracts not provided in the financial statements	**5.9**	6.1
Future commitments to purchase fuel under fixed and variable priced contracts	**5,194.4**	4,739.0

The contractual maturity of the future commitments to purchase fuel are as follows:

	As at 31 December	
	2016 £m	2015 £m
Within one year	**873.7**	870.5
Within two to five years	**2,773.0**	2,440.7
After five years	**1,547.7**	1,427.8
	5,194.4	4,739.0

Commitments to purchase fuel reflect long-term forward purchase contracts with a variety of international suppliers, primarily for the delivery of sustainable wood pellets for use in electricity production at Drax Power Station over the period from 2017–2027. To the extent these contracts relate to the purchase of wood pellets, they are not reflected elsewhere in our financial statements owing to application of the "own-use" exemption from fair value accounting to such contracts (see note 7.2).

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

	As at 31 December	
	2016 £m	2015 £m
Within one year	**3.7**	8.0
Within two to five years	**10.8**	8.1
After five years	**5.2**	7.0
	19.7	23.1

SECTION 8:
REFERENCE INFORMATION

This section details reference information relevant to the accounts. Here we describe the general information about the Group (e.g. operations and registered office). We also set out the basis of preparation of the accounts and general accounting policies that are not specific to any one note.

8.1 General information

Drax Group plc (the Company) is incorporated in England and Wales under the Companies Act. The Company and its subsidiaries (together, the Group) have three principal activities:

– Electricity generation;
– Electricity supply to business customers; and
– Manufacturing of sustainable compressed wood pellets for use in electricity production.

The Group's activities are principally based within the UK, with the wood pellet manufacturing activities situated in the US. The Group also operates in the UK domestic heat market.

The address of the Company's registered office and principal establishment is Drax Power Station, Selby, North Yorkshire, YO8 8PH, United Kingdom. A full list of operating companies of the Group is disclosed in note 5 to the Company's separate financial statements, which follow these consolidated financial statements.

8.2 Basis of preparation

Adoption of new and revised accounting standards

A number of new and amended standards became effective for the first time in 2016. The Group adopted the following from 1 January 2016:

IAS 27 (amended) – Separate Financial Statements – applicable to annual reporting periods beginning on or after 1 January 2016.

Annual improvements to 2012–2014 Cycle – all amendments are effective for annual reporting periods beginning on or after 1 January 2016.

IAS 16 (amended) – Property, Plant and Equipment and IAS 38 (amended) Intangible Assets – applicable to annual reporting periods beginning on or after 1 January 2016.

IAS 1 (amended) – Presentation of Financial Statements – effective for annual reporting periods beginning on or after 1 January 2016.

IAS 19 (amended) – Defined Benefit Plans: Employee contributions – effective for annual reporting periods beginning on or after 1 February 2015.

IFRS 11 (amended) – Joint Arrangements – applicable to annual reporting periods beginning on or after 1 January 2016.

The adoption of these updates and amendments has not had a material impact on the financial statements of the Group.

At the date of authorisation of these financial statements, the following new or amended standards and relevant interpretations, which have not been applied in these financial statements, were in issue but not yet effective (and some of which were pending endorsement by the EU – marked by *):

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

IFRS 15 (including clarifications issued on 12 Aril 2016) – Revenue from Contracts with Customers – effective for annual reporting periods beginning on or after 1 January 2018.

IFRS 16 (amended) – Leases – effective for annual reporting 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.*

IAS 12 (amended) – Income Taxes – effective for annual reporting periods beginning on or after 1 January 2017.*

IAS 7 (amended) – Statement of Cash Flows – effective for annual periods beginning on or after 1 January 2017.*

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

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

Following endorsement by the EU, the Group expects to adopt IFRS 9 in line with the 1 January 2018 effective date. The adoption of this standard is not expected to have a material impact on the recognition or measurement of the Group's financial instruments. However, following adoption it is anticipated that more of the Group's forward purchase contracts will in future qualify for hedge accounting under the new standard than under the existing standard. This will likely result in a greater proportion of unrealised gains and losses being recognised in the hedge reserve and an associated reduction in income statement volatility.

The Group is in the process of completing a preliminary impact assessment for the adoption of IFRS 15, which is expected to be adopted in line with the effective date of 1 January 2018. Whilst further work is required, the Group expects to review and update its revenue recognition policies in light of the updated requirements. Based on the initial findings of this process, a material change to the quantum and timing of profitability is considered unlikely at this stage.

The Group has not yet concluded its initial impact assessment into the adoption of IFRS 16; however at this stage the standard is not expected to have a material impact on the recognition, measurement or presentation of amounts within the financial statements in respect of leases. The Group currently expects to adopt IFRS 16 in the period it becomes mandatory, subject to EU endorsement.

Adoption of the other standards in future periods is not expected to have a material impact on the financial statements of the Group.

8.3 Accounting policies

The accounting policies set out below are considered to be general to the financial statements and not covered by a specific note.

Foreign currency transactions

Transactions in foreign currencies are translated into sterling at the exchange rate ruling at the date of the transaction. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items are not retranslated.

Foreign exchange gains and losses are recognised in the income statement within finance costs.

Foreign operations

The assets and liabilities of foreign operations with a functional currency other than sterling are translated into sterling using published exchange rates at the reporting date. The income and expenditure of such operations are translated into sterling using the exchange rate prevailing at the date of the transaction. Foreign exchange gains and losses resulting from the retranslation of the operation's net assets and its results for the year are recognised in the Consolidated statement of comprehensive income.

8.4 Related party transactions

A related party is either an individual or entity with control or significant influence over the Group, or a company that is linked to us by investment (such as an associated company or joint venture). Our primary related parties are our key management personnel.

Remuneration of key management personnel

The remuneration of the directors and Executive Committee members, who are considered to be the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24 "Related Party Disclosures". Further information about the remuneration of individual directors, together with the directors' interests in the share capital of Drax Group plc, is provided in the audited part of the Remuneration Committee report.

	Years ended 31 December	
	2016 £000	2015 £000
Salaries and short-term benefits	**5,011**	4,552
Aggregate amounts receivable under share-based incentive schemes	**1,146**	1,651
Company contributions to money purchase pension schemes	**44**	33
	6,201	6,236

Amounts included in the table above reflect the remuneration of the 10 (2015: 11) members of the Board and Executive Committee as described on pages 68 to 71, in addition to two former members of the Board and Executive Committee who resigned from the Board during 2016.

Amounts receivable under incentive schemes represents the expenses arising from share-based payments included in the income statement, determined based on the fair value of the related awards at the date of grant (note 6.2), as adjusted for non-market related vesting conditions.

There were no other transactions with directors for the periods covered by these consolidated financial statements.

COMPANY BALANCE SHEET

	Notes	As at 31 December 2016 £000	 2015 £000
Fixed assets			
Investment in subsidiaries	5	**706,894**	701,728
Current assets			
Amounts due from other Group companies		**6,300**	2,903
Cash at bank and in hand		**668**	571
		6,968	3,474
Current liabilities			
Amounts due to other Group companies		**(12,586)**	(10,220)
Net current liabilities		**(5,618)**	(6,746)
Net assets		**701,276**	694,982
Capital and reserves			
Called-up share capital	6	**46,951**	46,936
Capital redemption reserve		**1,502**	1,502
Share premium account		**424,244**	424,201
Profit and loss account		**228,579**	222,343
Total equity shareholders' funds		**701,276**	694,982

The Company reported a profit for the financial year ended 31 December 2016 of £12.1 million (2015: £52.0 million).

These financial statements were approved by the Board of directors on 15 February 2017.

Signed on behalf of the Board of directors:

Dorothy Thompson CBE
Chief Executive
15 February 2017

Will Gardiner
Chief Financial Officer
15 February 2017

COMPANY STATEMENT OF CHANGES IN EQUITY

	Share capital £000	Capital redemption reserve £000	Share premium £000	Profit and loss account £000	Total £000
At 1 January 2015	46,764	1,502	422,882	215,001	686,149
Share capital issued (note 6)	172	–	1,319	–	1,491
Profit and total comprehensive income for the year	–	–	–	51,986	51,986
Credited to equity for share-based payments	–	–	–	5,300	5,300
Equity dividends paid (note 8)	–	–	–	(49,944)	(49,944)
At 1 January 2016	46,936	1,502	424,201	222,343	694,982
Share capital issued (note 6)	**15**	**–**	**43**	**–**	**58**
Profit and total comprehensive income for the year	**–**	**–**	**–**	**12,064**	**12,064**
Credited to equity for share-based payments	**–**	**–**	**–**	**5,152**	**5,152**
Equity dividends paid (note 8)	**–**	**–**	**–**	**(10,980)**	**(10,980)**
At 31 December 2016	**46,951**	**1,502**	**424,244**	**228,579**	**701,276**

NOTES TO THE COMPANY FINANCIAL STATEMENTS

1. Basis of preparation

The separate financial statements of the Company are presented as required by the Companies Act 2006.

The Company meets the definition of a qualifying entity under Financial Reporting Standard 100 (FRS 100) issued by the Financial Reporting Council (FRC).

The financial statements have been prepared in accordance with FRS 101 (incorporating the Amendments to FRS 101 issued by the FRC in July 2015 and July 2016 and the amendments to Company law made by the Companies, Partnerships and Groups (Accounts and Reports) Regulations 2015).

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to presentation of a cash flow statement, standards not yet effective and certain related party transactions. Where required, equivalent disclosures are given in the consolidated financial statements.

The financial statements have been prepared under the historical cost convention. The principal accounting policies adopted are summarised below, and have been consistently applied to both years presented.

2. Summary of significant accounting policies

(A) Fixed asset investments

Fixed asset investments in subsidiaries are stated at cost less, where relevant, provision for impairment.

(B) Financial instruments

Issued equity – Ordinary shares are classified as equity as evidenced by their residual interest in the assets of the Company after deducting all of its liabilities. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds. The share premium account records amounts by which the proceeds from issuing shares exceeds the nominal value of the shares issued unless merger relief criteria within the Companies Act (2006) are met, in which case the difference is recorded in retained earnings.

Cash and cash equivalents – Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

3. Critical accounting judgements

(A) Critical judgements in applying the Company's accounting policies

The critical accounting judgements, to the extent they apply to the Company, are consistent with those of the Group described on page 117.

(B) Impairment of fixed asset investments

Determining whether the Company's investments in subsidiaries have been impaired requires estimates of the investment's values in use. The methodology for calculation of value in use is consistent with that of the Group, as described on page 130.

4. Profit and loss account

As permitted by Section 408 of the Companies Act 2006, the Company has elected not to present its own profit and loss account for the year. The Company's profit and loss account was approved by the Board on 15 February 2017. The profit attributable to the Company is disclosed as a footnote to the Company's balance sheet on page 167.

The Company received dividend income from its subsidiary undertakings totalling £14.7 million in 2016 (2015: £54.5 million).

The Company has no employees other than the directors, whose remuneration was paid by a subsidiary undertaking and a proportion was recharged to the Company.

The auditor's remuneration for audit services provided to the Company for the year ended 31 December 2016 was £20,000 (2015: £20,000).

5. Fixed asset investments

	Years ended 31 December	
	2016 £000	2015 £000
Carrying amount:		
At 1 January	**701,728**	692,272
Acquisition of Billington Bioenergy Limited	**–**	4,034
Capital contribution	**5,166**	5,422
At 31 December	**706,894**	701,728

5. Fixed asset investments continued

Investments in subsidiary undertakings

The capital contribution relates to the share-based payment charge associated with the Savings-Related Share Option Plan and Bonus Matching Plan schemes, which arises because the beneficiaries of the scheme are employed by subsidiary companies. For more information see note 6.2 to the consolidated financial statements.

Full list of subsidiary undertakings

The table below lists the Company's direct and indirect subsidiary undertakings as at 31 December 2016:

Name and nature of business		Country of incorporation and registration	Type of share	Group effective shareholding
Drax Group plc	Ultimate parent (holding) company	England and Wales	Ordinary	100%
Abergelli Power Limited	Development company	England and Wales	Ordinary	100%
Amite BioEnergy LLC	Trading company, fuel supply	Delaware, USA	Common	100%
Baton Rouge transit LLC	Trading company, fuel supply	Delaware, USA	Common	100%
Billington Bioenergy Limited	Trading company, fuel supply	England and Wales	Ordinary	100%
DBI O&M Company LLC	Non-trading company	Delaware, USA	Common	100%
Drax Biomass Inc.	Holding company	Delaware, USA	Common	100%
Drax Biomass Holdings Limited	Holding company	England and Wales	Ordinary	100%
Drax Biomass Holdings LLC	Holding company	Delaware, USA	Common	100%
Drax Biomass International Holdings LLC	Holding company	Delaware, USA	Common	100%
Drax Biomass (Immingham) Limited	Non-trading company	England and Wales	Ordinary	100%
Drax Biomass Transit LLC	Holding company	Delaware, USA	Common	100%
Drax CCS Limited	Holding company	England and Wales	Ordinary	100%
Drax Developments Limited (formerly Drax Biomass Developments Limited)	Holding company	England and Wales	Ordinary	100%
Drax Finance Limited	Holding company	England and Wales	Ordinary	100%
Drax Fuel Supply Limited	Trading company, fuel supply	England and Wales	Ordinary	100%
Drax GCo Limited	Non-trading company	England and Wales	Limited by Guarantee	100%
Drax Generation (Selby) Limited	Non-trading company	England and Wales	Ordinary	100%
Drax Group Holdings Limited	Holding company	England and Wales	Ordinary	100%
Drax Group Project Services Limited	Non-trading company	England and Wales	Ordinary	100%
Drax Group Services Limited	Trading company, administration services	England and Wales	Ordinary	100%
Drax Holdings Limited	Holding company	Cayman Islands	Ordinary	100%
Drax (International) Limited	Holding company	England and Wales	Ordinary	100%
Drax Ouse	Dormant company	England and Wales	Ordinary	100%
Drax Pension Trustees Limited	Non-trading company	England and Wales	Ordinary	100%
Drax Power Limited	Trading company, power generation	England and Wales	Ordinary	100%
Haven Heat Limited	Non-trading company	England and Wales	Ordinary	100%
Haven Power Limited	Trading company, power retail	England and Wales	Ordinary	100%
Haven Power Nominees Limited	Non-trading company	England and Wales	Ordinary	100%
Hirwaun Power Limited	Development company	England and Wales	Ordinary	100%
Millbrook Power Limited	Development company	England and Wales	Ordinary	100%
Morehouse BioEnergy LLC	Trading company, fuel supply	Delaware, USA	Common	100%
Progress Power Limited	Development company	England and Wales	Ordinary	100%

Drax Group plc directly holds 100% of the equity of Drax Group Holdings Limited. All other investments are held indirectly.

5. Fixed asset investments continued

All subsidiary undertakings operate in their country of incorporation. All subsidiary undertakings incorporated in England and Wales have their registered office at Drax Power Station, Selby, North Yorkshire, YO8 8PH. The registered office for Drax Holdings Limited is c/o Intertrust Corporate Services (Cayman) Limited, 190 Elgin Avenue, George Town, Grand Cayman KY1-9005, Cayman Islands. The principal business address for all subsidiaries incorporated in the USA is 5 Concourse Parkway, Suite 3100, Atlanta, GA 30328.

All subsidiary undertakings have 31 December year ends except Abergelli Power Limited, Hirwaun Power Limited, Millbrook Power Limited and Progress Power limited, which have 31 March year ends.

Subsequent to the year end, but before the date these financial statements were approved, Drax Developments Limited acquired 100% of the issued equity of Opus Energy Group Limited as described in note 5.1 to the consolidated financial statements. In addition to those listed in the table above, as of 10 February 2017 the Company also indirectly holds 100% of the shareholding of Opus Energy Group Limited, Opus Energy Limited, Opus Energy (Corporate) Limited, Opus Gas Supply Limited, Opus Energy Resources Limited, Farmoor Energy Limited, Abbott Debt Recovery Limited and Donnington Energy Limited. All of the acquired subsidiaries have their registered office at Lambourne House, 311–321 Banbury Road, Oxford, OX2 7JH.

6. Called-up share capital

	As at 31 December	
	2016 £000	2015 £000
Authorised:		
865,238,823 ordinary shares of 11 16/29 pence each	**99,950**	99,950
Issued and fully paid:		
2015 – 406,700,321 ordinary shares of 11 16/29 pence each	**46,951**	46,936
	46,951	46,936

The movement in allotted and fully paid share capital of the Company during the year was as follows:

	Years ended 31 December	
	2016 (number)	2015 (number)
At 1 January	**406,317,162**	404,821,561
Issued under employee share schemes	**383,159**	1,495,601
At 31 December	**406,700,321**	406,317,162

The Company has only one class of shares, which are ordinary shares of 11 16/29 pence each, carrying no right to fixed income. No shareholders have waived their rights to dividends.

Issued under employee share schemes

On 6 January a total of 30,081 shares were issued on early vesting of the Group's Bonus Matching Plan by one individual whose employment had terminated and discretion was used to exercise the shares. On 29 February 335,856 shares were issued in satisfaction of shares vesting in accordance with the rules of the Group's Bonus Matching Plan. Throughout May to December a total of 17,222 shares were issued in satisfaction of options vesting in accordance with the rules of the Group's Savings-Related Share Option Plan.

7. Distributable reserves

Note 8 sets out the proposed final dividend of £11 million in respect of 2016.

The Company considers its distributable reserves to be comprised of the profit and loss account with a total value of £229 million. Accordingly the Company considers itself to have sufficient distributable profits from which to pay the current year final dividend. Based on a total dividend for 2016 of £11 million, the Company has sufficient distributable reserves to pay 20 years of dividend at the current level without generating further distributable profits.

The Company is dependent upon its subsidiaries for the provision of cash with which to make dividend payments. As shown in note 4.2 to the consolidated financial statements the Group has sufficient cash resources with which to meet the proposed dividend.

8. Dividends

	Years ended 31 December	
	2016 £m	2015 £m
Amounts recognised as distributions to equity holders in the year (based on the number of shares in issue at the record date):		
Interim dividend for the year ended 31 December 2016 of 2.1 pence per share paid on 7 October 2016 (2015: 5.1 pence per share paid on 9 October 2015)	**8.6**	20.7
Final dividend for the year ended 31 December 2015 of 0.6 pence per share paid on 13 May 2016 (2015: 7.2 pence per share paid on 15 May 2015)	**2.4**	29.2
	11.0	49.9

At the forthcoming Annual General Meeting the Board will recommend to shareholders that a resolution is passed to approve payment of a final dividend for the year ended 31 December 2016 of 0.4 pence per share (equivalent to approximately £1.8 million) payable on or before 12 May 2017. The final dividend has not been included as a liability as at 31 December 2016.

9. Contingent liabilities

The Company has provided unsecured guarantees to third parties in respect of contracts held by a subsidiary company. The guarantees have been issued for £nil consideration and the Company has not charged the subsidiary for the guarantees.

The Company has granted a charge over the assets of certain of its subsidiaries, in respect of the Group's debt (detailed in note 4.3 to the consolidated financial statements), which is guaranteed and secured directly by each of the subsidiary undertakings of the Company that is party to the security arrangement. The Company itself is not a guarantor of the Group's debt.

SHAREHOLDER INFORMATION

Key dates for 2017

At the date of publication of this document, the following are the proposed key dates in the 2017 financial calendar:

Annual General Meeting	13 April
Ordinary shares marked ex-dividend	20 April
Record date for entitlement to the final dividend	21 April
Payment of final dividend	12 May
Financial half year end	30 June
Announcement of half year results	19 July
Financial year end	31 December

Other significant dates, or amendments to the proposed dates above, will be posted on the Company's website as and when they become available.

Results announcements

Results announcements are issued to the London Stock Exchange and are available on its news service. Shortly afterwards, they are available under "Regulatory news" within the Investor section on the Company's website.

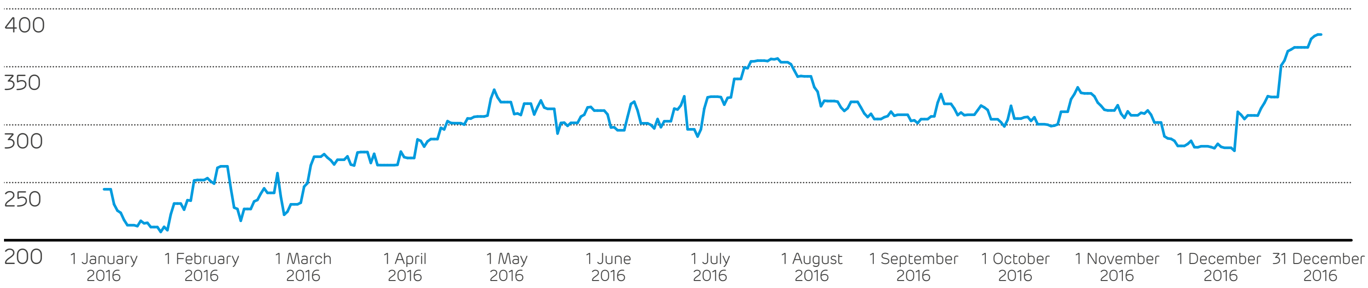
Share price

Shareholders can access the current share price of Drax Group plc ordinary shares on our website at www.drax.com. During London Stock Exchange trading hours the price shown on the website is subject to a delay of approximately 15 minutes and outside trading hours it is the last available price.

The table below provides an indication of the fluctuations in the Drax Group plc share price during the course of 2016, and the graph provides an indication of the trend of the share price throughout the year.

Closing price on 31 December 2015	Low during the year (18 January 2016)	High during the year (30 and 31 December 2016)	Closing price on 31 December 2016
244.4 pence	207.6 pence	377.9 pence	377.9 pence

Share price 2016 (pence)



Note:
The share prices given are the middle market closing prices as derived from the London Stock Exchange Daily Official List.

Market capitalisation
The market capitalisation, based on the number of shares in issue and the closing price at 31 December 2016, was approximately £1,536 million (2015: £993 million).

Financial reports
Copies of all financial reports we publish are available from the date of publication and can be downloaded from our website. Printed copies of reports can be requested by writing to the Company Secretary at the registered office, by clicking on "Contact Us" on our website, or direct by e-mail to enquiries@drax.com

Drax shareholder queries
Drax's share register is maintained by Equiniti Limited ("Equiniti"), who is primarily responsible for updating the share register and for dividend payments.

Shareholders should contact Equiniti directly if they have a query relating to their Drax shareholding, in particular queries regarding:

- transfer of shares;
- change of name or address;
- lost share certificates;
- lost or out-of-date dividend cheques;
- payment of dividends direct to a bank or building society account; and
- death of a registered shareholder.

Equiniti can be contacted as follows:

- Call Equiniti 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.
- Write to Equiniti at Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA.

When contacting Equiniti by telephone or in writing it is advisable to have your shareholder reference to hand and quote Drax Group plc, as well as the name and address in which the shares are held.

Online communications
Registering for online communications allows you to have more control over the administration of your shareholding. The registration process is easy via Equiniti's secure website www.shareview.co.uk

Once registered with Shareview you are able to:

- elect how Drax communicates with you;
- amend some of your personal details;
- amend the way you receive dividends; and
- buy or sell shares online.

Registering for electronic communications does not mean that you can no longer receive paper copies of documents. We are able to offer a range of services and tailor the communications to meet your needs.

A range of frequently asked shareholder questions can also be found on the Drax website at www.drax.com/investors/faq

Tax on dividends
In the 2015 Budget, the Chancellor announced changes in the way that dividends would be taxed in the future. Below is a brief summary of the guidance provided by HMRC. If you are in any doubt as to the impact on your personal circumstances, you are recommended to seek your own financial advice from a professional adviser authorised under the Financial Services and Markets Act 2000.

From April 2016, there was an income tax charge on dividends at the rate of 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

The long-standing system of tax credits attached to dividends was replaced with a new tax-free Dividend Allowance. This means that there is no tax to pay on the first £5,000 of dividend income, no matter what non-dividend income a shareholder may have. Dividends paid on shares held within pensions and ISAs will be unaffected, remaining tax-free.

Non-taxpayers and basic rate taxpayers who receive dividend income between £5,001 and £10,000 will need to make a declaration (to HMRC) for the first time. Individuals with dividend income of more than £10,000 are already required to be in HMRC's Self-Assessment regime. The impact on Share Incentive Plan participants receiving cash dividends on their plan shares align with those for Shareholders. Further information and updates on tax on dividends can be found on the HMRC website at www.gov.uk/tax-on-dividends/overview

As the Dividend Tax Credit will no longer be required it is expected that a dividend confirmation will still need to be sent to shareholders to replace the old "tax voucher". The Company is currently considering whether to move to the practice of issuing just one dividend confirmation document towards the end of the tax year, irrespective of the number of cash payments made during the course of the year, rather than issuing a document each time a dividend is paid. Shareholders will be advised of the outcome in due course.

Beneficial owners and "information rights"
If your shares are registered in the name of a third party (i.e. an ISA provider or other nominee company) you may, if you wish, receive information rights under Section 146 of the Companies Act 2006. In order for this to happen, you must contact the third party registered holder, who will then nominate you. All communications by beneficial owners of shares where the shares are held by third party registered holders must be directed to that registered holder and not to Drax or Equiniti.

ShareGift
ShareGift (registered charity No. 1052686) is an independent charity which provides a free service for shareholders wishing to dispose charitably of small parcels of shares, which would most likely cost more to sell than they are worth. There are no capital gains tax implications (i.e. no gain or loss) on gifts of shares to charity and it is possible to obtain income tax relief. Further information can be obtained directly from the charity at www.sharegift.org

Share frauds ("Boiler room scams")
In recent years, many companies have become aware that their shareholders have received unsolicited phone calls or correspondence offering to purchase their shares at apparently inflated prices. It is often the case that the caller, or message in the correspondence claims that they represent a majority shareholder who is looking to take over the Company. At the time of this report, the Company was not the subject of a take-over attempt, hostile or otherwise, and approaches such as those outlined are usually made by unauthorised companies and individuals. Shareholders should be very wary of any unsolicited advice, offers to buy shares at a premium or offers of free reports into the Company. Below is the advice from the Financial Conduct Authority (the "FCA").

Beware of share fraud
Fraudsters use persuasive and high-pressure tactics to lure investors into scams. They may offer to sell shares that turn out to be worthless or non-existent, or to buy shares at an inflated price in return for upfront payment. While high profits are promised, if you buy or sell shares in this way you will probably lose your money.

How to avoid share fraud:

- Keep in mind that firms authorised by the FCA are unlikely to contact you out of the blue with an offer to buy or sell shares.
- Do not get into a conversation, note the name of the person and firm contacting you and then end the call.
- Check the Financial Services Register from www.fca.org.uk to see if the person and firm contacting you is authorised by the FCA.
- Beware of fraudsters claiming to be from an authorised firm, copying its website or giving you false contact details.
- Use the firm's contact details listed on the Register if you want to call it back.
- Call the FCA on 0800 111 6768 if the firm does not have contact details on the Register or you are told they are out of date.
- Search the list of unauthorised firms to avoid at www.fca.org.uk/scams
- Consider that if you buy or sell shares from an unauthorised firm you will not have access to the Financial Ombudsman Service or Financial Services Compensation Scheme.
- Think about getting independent financial and professional advice before you hand over any money.

Remember, if it sounds too good to be true, it probably is!

Report a scam
If you are approached by fraudsters please tell the FCA using the share fraud reporting form at www.fca.org.uk/scams, where you can find out more about investment scams.

You can also call the FCA Consumer Helpline on 0800 111 6768.

If you have already paid money to share fraudsters you should contact Action Fraud on 0300 123 2040.

COMPANY INFORMATION

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Registration details
Registered in England and Wales
Company Number: 5562053

Company Secretary
David McCallum

Enquiry e-mail address
enquiries@drax.com

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Remuneration advisers
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1 Embankment Place, London WC2N 6RH

Solicitors
Slaughter and May LLP
One Bunhill Row, London EC1Y 8YY

GLOSSARY

Advantaged fuels
Fuel that gives a price advantage against standard bituminous coals. Such fuels include pond fines, off-specification coal and petcoke.

Ancillary services
Services provided to national grid used for balancing supply and demand or maintaining secure electricity supplies within acceptable limits, for example Black Start contracts. They are described in Connection Condition 8 of the Grid Code.

Availability
Average percentage of time the units were available for generation.

Average achieved price
Power revenues divided by volume of net sales (includes imbalance charges).

Balancing mechanism
The sub-set of the market through which the system operator can call upon additional generation/consumption or reduce generation/consumption through market participants' bids and offers, in order to balance the system minute-by-minute.

Bark spread
The difference between the power price and the cost of biomass, net of renewable support.

Carbon price support mechanism (or carbon price floor or carbon tax)
A tax upon fossil fuels (including coal) used to generate electricity. It is charged as a levy on coal delivered to the power station.

Contracts for difference (CfD)
A mechanism to support investment in low-carbon electricity generation. The CfD works by stabilising revenues for generators at a fixed price level known as the "strike price". Generators will receive revenue from selling their electricity into the market as usual. However, when the market reference price is below the strike price they will also receive a top-up payment from suppliers for the additional amount. Conversely if the reference price is above the strike price, the generator must pay back the difference.

Dark green spread
The difference between the power price and the cost of coal and carbon, including CO_2 allowances under the EU Emissions Trading Scheme and the UK Carbon Price Support (CPS) Mechanism.

Department for Business, Energy and Industrial Strategy (BEIS)
The Government department bringing together the responsibilities for business, industrial strategy, science, innovation, energy and climate change (formerly DECC).

EBITDA
Profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.

EU ETS
The EU Emissions Trading System is a mechanism introduced across the EU to reduce emissions of CO_2; the scheme is capable of being extended to cover all greenhouse gas emissions.

Feed-in tariff
A long-term contract set at a fixed level where variable payments are made to ensure the generator receives an agreed tariff. The feed-in tariff payment would be made in addition to the generator's revenues from selling in the market.

Forced outage
Any reduction in plant availability, excluding planned outages.

Forced outage rate
The capacity which is not available due to forced outages or restrictions expressed as a percentage of the maximum theoretical capacity, less planned outage capacity.

Grid charges
Includes transmission network use of system charges (TNUoS), balancing services use of system charges (BSUoS) and distribution use of system charges (DUoS).

IFRSs
International Financial Reporting Standards.

LECs
Levy Exemption Certificates. Evidence of CCL exempt electricity supplies generated from qualifying renewable sources.

Levy control framework
A control framework for BEIS (formerly DECC) levy-funded spending intended to make sure that BEIS achieves its fuel poverty, energy and climate change goals in a way that is consistent with economic recovery and minimising the impact on consumer bills.

Load factor
Net sent out generation as a percentage of maximum sales.

Lost time injury rate (LTIR)
The frequency rate is calculated on the following basis: lost time injuries/hours worked x 100,000. Lost time injuries are defined as occurrences where the injured party is absent from work for more than 24 hours.

Net balancing mechanism
Net volumes attributable to accepted bids and offers in the balancing mechanism.

Net cash/(debt)
Comprises cash and cash equivalents, short-term investments less overdrafts and borrowings net of deferred finance costs.

Net sales
The aggregate of net volumes attributable to bilateral contracts, power exchange trades and net balancing mechanism.

Net sales at notional balancing point (NBP)
Net sales at NBP is the volume of power sold to customers by our Retail business expressed at the NBP. The NBP reflects the volume of power sold before deduction of transmission and distribution losses incurred in transporting this power from the grid to the customer meter.

Planned outage
A period during which scheduled maintenance is executed according to the plan set at the outset of the year.

Planned outage rate
The capacity not available due to planned outages expressed as a percentage of the maximum theoretical capacity.

Power exchange trades
Power sales or purchases transacted on the APX UK power trading platform.

ROCs
A Renewable Obligation Certificate ("ROC") is a certificate issued to an accredited generator for electricity generated from eligible renewable sources. The Renewable Obligation (RO) is currently the main support scheme for renewable electricity projects in the UK.

Summer
The calendar months April to September.

System operator
National Grid Electricity Transmission. Responsible for the coordination of electricity flows onto and over the transmission system, balancing generation supply and user demand.

Total recordable injury rate (TRIR)
The frequency rate is calculated on the following basis: (lost time injuries + worse than first aid injuries)/hours worked x 100,000.

UK NAP
UK National Allocation Plan.

Underlying financial measures
We report financial measures described as "underlying" such as profit after tax and earnings per share. Underlying measures are adjusted to exclude the impact of gains and losses on derivative contracts and the associated tax.

Winter
The calendar months October to March.

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