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○ **Drax Group plc**
Annual Report and Accounts 2005



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- Drax Group plc is the ultimate holding company of Drax Power Limited, the owner of Drax Power Station, situated at Selby, North Yorkshire. Drax Power Station is the largest, cleanest and most efficient coal-fired power station in the UK. The total output capacity of the Station's six generators is 3,960MW. All units are fitted with flue gas desulphurisation equipment, which removes at least 90% of the sulphur dioxide from emissions. Drax sells the electricity it generates into the physical wholesale power market for Great Britain, and at current output levels supplies some 7% of the country's electricity needs.

As well as being an important strategic asset nationally, Drax Power Station is also vital to the local economy. Drax Power employs some 620 people directly and, through its use of local sub-contractors and outsourcing, supports many other jobs indirectly in the Selby area. It is also the major customer for a number of the UK's remaining coal mines.

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- **Drax Group plc** Following the delivery of strong improvements in operational and financial performance during 2005, Drax Group plc made its debut on the London Stock Exchange on 15 December 2005. A fitting end to a successful year for the business and the start of a new chapter in the history of Drax.

Highlights of 2005

- Refinancing and Listing of Drax Group plc successfully completed on 15 December 2005
- Revenue from generation up 55% at £849m
- Average capture price of electricity up 51% to £33.9/MWh
- Net sales of 23.2TWh; an increase of 0.3TWh
- Gross margin increased by 63% to £389m
- EBITDA increased by 166% to £239m
- Improved trading counterparty interest following enhanced credit status of the Group
- Best full year performance in forced outage rate since 1997
- Total recordable injury rate down by 39%

£849m

- Revenue from generation up by 55%

£33.9/MWh

- Average capture price increased by 51%

23.2TWh

- Net sales increased by 0.3TWh

£389m

- Gross margin increased by 63%

£239m

- EBITDA increased by 166%

	Years ended 31 December	
	2005 £'m	2004 £'m
Revenue from generation ⁽¹⁾	849	549
Total revenue	929	624
Gross margin ⁽²⁾	389	239
EBITDA ⁽³⁾⁽⁴⁾	239	90
EBITDA (after exceptional items) ⁽⁵⁾	385	90
Operating profit	354	55
Profit/(loss) before tax	264	(42)

(1) Revenue from generation excludes revenues associated with power purchases of £80m (2004: £75m).

(2) Gross margin is defined as total revenues less total fuel costs of £540m (2004: £385m).

(3) EBITDA is profit before interest, tax, depreciation and amortisation, exceptional items and unrealised losses on derivative contracts.

(4) Exceptional items in 2005 comprise income of £19m due to the reversal of provisions relating to impairment of tangible fixed assets and £311m as a result of three distributions received from the Administrators of TXU, partially offset by a charge under the Group's Long-Term Incentive Plan of £38m, and costs incurred with respect to the Refinancing and Listing of £29m. Unrealised losses on derivative contracts were £117m in 2005. There were no exceptional items in 2004.

(5) EBITDA (after exceptional items) is profit before interest, tax, depreciation and amortisation.

- more _____ Drax Power Station is the largest, cleanest and most efficient coal-fired power station in the UK. The output capacity of our six generators is 3,960MW, and we currently provide enough power to meet 7% of the UK's electricity needs.

more

Operations

"Running a power station the size of Drax is a massive operation in terms of the logistics of handling the variety of materials used in the day-to-day running of the plant, and controlling and scheduling the many different parts of the plant. We have a strong team in place to ensure we deliver high standards of reliability and availability."

Jason Shipstone
Materials Handling Manager

● **less** _____ At Drax we are committed to reducing the environmental impact of our operations. Our flue gas desulphurisation (FGD) equipment removes at least 90% of sulphur dioxide (SO₂) emissions and our programme to reduce emissions of oxides of nitrogen (NO_x) is well under way. We are also making important progress in reducing our emissions of carbon dioxide (CO₂) through co-firing renewable biomass materials.

less

Protecting the Environment

"We regard environmental issues as key to our business. We are committed to continuous improvement across our operations and work with all stakeholders to enhance our environmental performance and reduce the impact our operations have both locally and nationally."

Nigel Burdett
Head of Environment

- **internal** _____ The skills base of the workforce is wide and varied, and has been developed further over the last two years with an eye on the future needs of the business. We take pride in our short lines of communication between key areas of the business which enable us to respond quickly to changing market circumstances.

Health and Safety

"The nature and complexity of our operations means that health and safety at work is an absolute priority. Each member of our some 620 strong workforce has the right to work in a safe environment, and we work hard to make that right a reality."

Ernie Rowe
Safety Manager

internal

○ **external** _____ Drax has a significant presence in the local community. We contribute to the local economy both directly, through employment, and indirectly, through the many goods and services that we source. We are committed to being a good neighbour and work hard to maintain close relations with our community.

external

Caring for the Community

“We see thousands of different faces of all ages each year, all keen to learn more about what we do at Drax. Opening our doors to these people is an important part of achieving our aim to be a good neighbour.”

Pauline Butler
Station Guide

- **focused** _____ In optimising our performance we continually review work practices and procedures with the aim of achieving "best in class" results. Only in this way can we enhance our position as a leading power generator in the UK market and contribute towards fulfilling our commitment to maximise and deliver shareholder value.

focused

Improving Business Performance

"Despite having been in the business of power generation for many years, we are always looking for ways to improve our delivery and effectiveness. Through reviewing existing procedures and systems, and encouraging new ideas, we are able to deliver practical solutions and improve our business performance."

John Grimes
Maintenance Manager

- **expanding** _____ We seek to enhance revenue and improve profitability through the use of alternative fuels such as renewable biomass materials and petroleum coke. We will continue to drive the business forward through developing long-term contracts for our key commodities of fuel, power and CO₂ emissions allowances, and other long-term business enhancements.

expanding

Trading Floor

"We work closely with the operations side of the business continually seeking to optimise our positions in the three key commodities in which we deal and deliver value to the business. Keeping trained eyes on all aspects of the markets in which we trade enables us to take informed decisions when it comes to hedging our positions and delivering against our corporate targets."

Damien Speight
Head Trader

○ a year of transformation _____ As a result of a successful Refinancing and Listing the Group now enjoys a robust and simple capital structure appropriate to a business operating within commodity markets.

Gordon Horsfield
Chairman

Chairman's Statement

Introduction

Through the ownership of the largest, cleanest and most efficient coal-fired power station in the country, with a nominal output capacity of 3,960MW, the Group provides power sufficient to meet around 7% of the electricity needs of the UK.

The year 2005 was transformational: it saw the Group refinanced and its shares listed for the first time on the London Stock Exchange. Accordingly, this is the first Annual Report and Accounts for Drax Group plc which became the holding company of the Drax group of companies on 15 December 2005.

Refinancing and Listing

In March 2005, Drax Group Limited set out its proposals to refinance and list the business by the end of the year. The reasons were clear to the Board. The prevailing capital structure was restricting the ability of management to develop its trading and business strategy and in consequence management efforts to enhance shareholder value were being inappropriately constrained. Throughout the year in a series of investor roadshows, letters, meetings and discussions the Board outlined and developed its proposals to align the trading, operational, and financial strategies to deliver greater shareholder value. Much effort was put into engaging with investors, seeking their understanding of the plans, and receiving their feedback directly and through their representatives, all of which helped shape the final proposals. Whilst conceptually straightforward, the Refinancing and Listing were technically difficult to implement, requiring very high levels of positive shareholder and lender approvals within what was then a complex capital structure.

During the Autumn of 2005 three separate indicative offers were made for the business. The Board assessed each of them against the same criteria: value, deliverability and timeliness. Having regard to these criteria, and to the views expressed by investors directly, indirectly through their representatives, and significantly through their votes, the Board with the support of its advisers concluded that the Refinancing and Listing was the best option and the bids were either rejected or fell away.

The Group now enjoys a robust and simple capital structure appropriate to a business operating within commodity markets and its shares trade in a transparent and liquid market. I am pleased to note that the Refinancing and Listing delivered the expected investment grade ratings for the Group debt and for the principal operating subsidiary, Drax Power Limited. The resulting credit standing with trading counterparties, together with our enhanced ability to provide credit support where necessary, are already delivering significant trading and operational benefits.

Results for 2005

The Group produced a strong performance in 2005 delivering an operating profit (before exceptional items and mark-to-market adjustments on derivative contracts) of £208m, a substantial improvement on the previous year's performance. EBITDA of £239m was £19m better than the forecast £220m EBITDA (before exceptional items and mark-to-market adjustments on derivative contracts) included in our Listing Particulars which were published in October 2005 and updated on 11 November 2005. Including exceptional items and mark-to-market adjustments would increase both operating profit and EBITDA by £146m.

Returns to Shareholders

In our 2005 Listing Particulars the Company put forward Drax as a "cash conversion" story. It laid out its intention to make distributions to shareholders in the form of an annual base dividend of £50m (payable in line with normal listed company practice) and, in addition, to distribute substantially all of any remaining cash flow subject to the availability of reserves and after making provision for debt payments, debt service requirements (if any), capital expenditure, and other expected business requirements.

In respect of our base dividend, we intend to pay an interim dividend in respect of the six months to 30 June 2006 of 4 pence per share being approximately £16.3m. This will be paid in Autumn 2006.

As regards the additional distribution, work has commenced to identify the most appropriate method for returning surplus cash. We expect to advise shareholders of the proposed method of return at our Annual General Meeting in May, followed by an indication of the likely range of distribution, timing and any shareholder approval process in a trading update given at the end of June 2006.

Board Developments

In January 2005, Gordon Boyd joined the Board as Finance Director, from British Energy.

In April 2005, Gerald Wingrove, who had joined Drax with me in July 2003 and become Chief Executive in December that year, left the business. I should like to take this opportunity to acknowledge his contribution and to thank him for all his hard work.

In September 2005, we welcomed Dorothy Thompson as our new Chief Executive. Dorothy, formerly head of InterGen's UK and European business, brings to Drax her extensive knowledge of the power industry in general and of gas-fired generation in particular.

On 15 December 2005, Charles Berry and Jamie Dundas joined the Company as additional non-executive directors. Charles has extensive experience in the UK power sector, joining Drax from ScottishPower where he was appointed to the board in 1999. Jamie brings excellent City experience and experience from his current membership of the Boards of two FTSE 100 companies.

Each of the above Board appointments was made following a recruitment exercise carried out by external search consultants.


As foreshadowed in our Listing Particulars, my own role as executive Chairman came to an end on 7 March 2006 and is now that of a non-executive Chairman. The Board comprises eight directors: three executives and five non-executives, of which four are deemed to be independent under The Combined Code on Corporate Governance.

Investor Relations

In the course of the Refinancing and Listing process during 2005, and so as to keep the then current and potential investors informed of the progress of the business, we undertook four investor roadshows in both the UK and US, supplemented by formal investor presentations and a number of written communications. The benefits flowing from the high quality relationships developed with our then investor base have not been lost on the Board. Inevitably, since the Listing last December, there has been a material change in the composition of our shareholder register. We intend to maintain and develop the high standards for investor relations that we set ourselves in 2005. To this end we already have plans in place to meet our current major investors during March 2006.

Our People

The sustained commitment and dedication of all our employees has been a crucial part of our success over the last three years. The old and new skills brought to Drax combined as one team and their efforts against the backdrop of improving markets has seen the business develop strongly. Our people at Drax rose to the new challenges and opportunities posed by the impending Refinancing and Listing. I should like to thank all of them for their contribution, flexibility and enthusiasm in what proved to be an eventful and successful year.


Gordon Horsfield
Chairman
7 March 2006

○ **early returns realised** Investment in plant management and maintenance has delivered improved plant performance which directly translates into improved safety, availability and reliability.

Chief Executive's Statement

"To increase our flexibility to import coal, we increased our contracted port capacity in 2005. We have also worked with our rail freight suppliers to improve logistics between the ports and mines from which our coal is delivered."

Introduction

In 2005, commodity market developments dominated the UK energy landscape. Energy commodity prices have been strong, led by the price of crude oil. Natural gas prices were particularly high towards the end of the year, influenced by oil and a tighter demand/supply balance as the UK moved to a greater reliance on imported gas. High gas prices have meant that gas-fired generation became the principal price-setting plant in the power market and had a strong upward influence on the power price. The year also saw the introduction of the EU Emissions Trading Scheme with carbon becoming a traded commodity and a new cost to fossil fuelled power plant, so also influencing the price of power upwards.

Against this background of strong commodity markets, Drax began to realise some early returns from investments in plant management and maintenance. The improvement of plant performance compared to 2004 was very positive and directly translated into improved safety, availability and reliability.

Energy Sales and Other Income

In the year, Drax Power made net sales of 23.2TWh (2004: 22.9TWh) of electricity at an average capture price of £33.9/MWh (2004: £22.5/MWh). The capture price achieved reflects the impact of power sold forward in 2003 and 2004 for delivery in 2005, as well as market prices prevailing in 2005.

Power prices rose significantly during 2005 as reflected in the Drax capture price. For example, the price of the forward contract for power delivered in the six months starting October 2005 rose 49% between the beginning of the year and the start of delivery in October.

Drax makes sales of other products and services as well as contracted power. These include ancillary services provided to the national grid, Renewables Obligation Certificates (ROCs), Levy Exemption Certificates (LECs), Sulphur Emissions Allowances and marketable by-products from our generating activities, namely ash and gypsum. In 2005, these activities generated net sales of £32m.

Fuel Procurement

COAL

Drax burnt approximately 9.3 million tonnes of coal in 2005, with around 60% being sourced from the

Dorothy Thompson
Chief Executive

UK and 40% internationally. During 2005, we paid an average price of £37.3/tonne (2004: £32.7/tonne) for our coal, including the cost of delivery to the power station. International coal prices fell from a peak of US\$75/tonne early in the year to about US\$54/tonne at the close.

To increase our flexibility to import coal we increased our contracted port capacity in 2005. We have also worked with our rail freight suppliers to improve logistics between the ports and mines from which our coal is delivered.

BIOMASS - NATURALLY GROWN FUEL

As well as coal, Drax burns renewable biomass material which has the twin benefits of reducing CO₂ emissions and providing an additional revenue source through the sales of ROCs and LECs. During 2005 we burnt over 230,000 tonnes of biomass compared with 95,000 tonnes in 2004. We made significant progress during the year in the development of energy crops to be grown by local farmers. Contracts are being arranged to grow and to deliver energy crops over the next decade. Work continues to source additional energy crops and other cost effective biomass.

EMISSIONS

On 1 January 2005 the EU Emissions Trading Scheme in respect of CO₂ emissions allowances was implemented. Phase I of the scheme covers 2005-2007 and Phase II will cover 2008-2012. Drax has an annual allocation granted by the UK Government of 14.55 million tonnes of allowances in Phase I. In 2005 we purchased a further 6.3 million tonnes of allowances as power was generated at volumes beyond those supported by the allocation. Carbon prices rose through 2005, opening the year at around €8/tonne and closing at over €20/tonne.

In October 2005, new Integrated Pollution Prevention and Control regulations were implemented which allow the trading of allowances for certain emissions including SO₂ and NO_x. Drax's allocation of SO₂ and NO_x allowances for 2005 were sufficient to cover generation. No purchases were required. Indeed, as Drax is fully equipped with flue gas desulphurisation, optimisation of emissions has resulted in tradeable surplus SO₂ allowances. In 2005, Drax completed the first SO₂ trade and continues to transact in the market.

We transacted several structured deals in 2005 which combined sales of power with purchases of coal and, in some instances, carbon on a forward basis for up to two years.

For planned outages, a milestone planning process has been implemented and has already resulted in some performance improvements.

"Last year saw improvements in both the planned and forced outage rates, with a strong downward trend in forced outage rate over the four quarters of 2005, resulting in the best full year performance since 1997."

87.2%

- The availability for 2005 was 87.2% compared to 81.3% in 2004

Trading

The trading function covers all the commodity aspects of our operations including power, fuel, CO₂ emissions allowances, renewable generation incentives, and grid services. The principal objectives of our trading strategy are to optimise the physical inputs and outputs of the plant, and to enhance the value of the business while delivering some stability in value through commodity price cycles. An important aspect of capturing value is exploiting the optionality of the power plant through its flexibility.

In the short term, our trading strategy focuses on ensuring that our output is sold, in a way that adds value to market prices, for each period where market prices exceed our marginal cost of production. In the liquid forward power market, which generally trades over two Winter and two Summer seasons, our objective is to capture better than market power prices whilst making steady sales across a range of counterparties and hedging the related coal and CO₂ emissions allowances requirements of the power sales.

In the medium to long term our objective is to transact deals, at attractive prices, that provide a hedge to the business. We transacted several structured deals in 2005 which combined sales of power with purchases of coal and, in some instances, carbon on a forward basis for up to two years.

Drax's access to commodity markets was greatly constrained during the year by the relatively poor credit status of Drax Power Limited, the trading counterparty. This was a result of the high leverage of the Drax Group. On the Refinancing of the Group on 15 December 2005, the credit status of Drax Power Limited was greatly improved as reflected in the investment grade rating granted to the entity by Standard & Poor's.

Operations

HEALTH AND SAFETY

Health and safety remains our highest priority. The year 2005 was the first full year operating the DuPont™ STOP™ behaviour based safety system which we have implemented as a vehicle to deliver a step change in safety culture. In addition we have focused on developing simple and clear systems, improved communication, detailed safety incident reporting and follow-up, and we have introduced weekly safety meetings for all operational staff. The contractor interface has been strengthened with a

dedicated team from Drax. Overall, recordable personal injury rates have reduced by 39% compared to 2004.

LOAD FACTOR AND AVAILABILITY

The plant load factor for the year was 73.9% before net power purchases (2004: 69.1% after net power purchases) with an availability of 87.2% (2004: 81.3%). We only seek to generate electricity when it is profitable to do so. Thus we target profitability rather than production volumes. A key performance metric for the plant is availability. Last year saw improvements in both the planned and forced outage rates, with a strong downward trend in forced outage rate over the four quarters of 2005, resulting in the best full year performance since 1997. The forced outage reduction programme has included the establishment of cross functional reliability teams focused on specific plant areas in the first quarter of 2005 and the adoption of data driven processes to analyse historic failures to deliver improvements in reliability. For planned outages, a milestone planning process has been implemented and has already resulted in some performance improvements. An integrated Drax/contractor outage planning team was established during the final quarter of 2005 with a view to securing further performance improvements in 2006 and beyond.

INVESTMENT IN OPERATIONS

We continue to invest in plant and equipment with four main objectives in mind: to meet future environmental and safety legislative requirements; to facilitate fuel diversity; to support reductions in the forced outage rate; and to improve plant efficiency.

To meet the 2008 Large Combustion Plant Directive ("LCPD") requirements for oxides of nitrogen emissions standards we have a programme to install Boosted Over Fire Air ("BOFA") equipment on each of the six units. During 2005, two units have had BOFA installed; one of the units has been commissioned and has successfully completed all of its performance tests, meeting in full the design specification. Construction will start in 2006 to install BOFA systems on the remaining four units in time for the 2008 change. New process control systems, together with BOFA and new instrumentation, designed to deliver continuous emissions monitoring across the units, will ensure compliance with LCPD limits for oxides of sulphur and nitrogen, and particulates.

Co-firing renewable biomass materials with coal in our existing boilers is already delivering significant savings in emissions of CO₂, and, but, given the right energy policy framework, it could deliver much more.

Fuel diversity projects include petroleum coke ("petcoke") and biomass. Drax has invested in petcoke handling and blending facilities during the year and commenced an 18 month trial burn on one unit in June 2005. Air quality monitoring, both before and during the trial, has shown that there has been no material increase in pollutants measured. We expect to apply for a licence for commercial burn commencing in 2007. Although the early results from the trials are encouraging, there can be no guarantee that permission to burn petcoke in some or all of the units will be granted. A biomass "direct injection" system was installed on one unit during August 2005 and has proved to be an effective way of delivering larger volumes of prepared biomass to the boiler than is possible through the coal pulverising mills. Drax has the potential to install, at modest cost, such a system on each unit, should the investment criteria be met.

Forced outage rate support has involved selective investment in boiler parts and tubes, milling equipment, flue gas desulphurisation plant, conveyors, common plant equipment and infrastructure and strategic spares, as part of the programme to drive down forced outage rates to the levels achieved in the early 1990s.

Drax recognises the potential to improve operating and thermal efficiency leading to reduced fuel costs and emission rates. Examples of work undertaken in 2005 are investment in the flue gas desulphurisation facility to improve scrubbing efficiency and a project to improve boiler heat transfer when burning imported coal. Drax is also exploring several turbine enhancements and feed system upgrades with the objective of further improving efficiency and reducing consumption.

Regulatory Matters

ENERGY REVIEW

On 23 January 2006, the UK Government launched its Energy Review ("the Review"). The Review promises to be broad in scope, considering both energy supply and demand and, importantly, within that, all energy sources for power generation. We welcome the Review as an opportunity to increase awareness of the need for coal-fired generation in the long-term energy mix of the country. Given the right policy framework, we believe that coal-fired generation can contribute to the Government's key energy policy objectives of delivering security of supply and

affordability, and tackling climate change. We are fully engaged with the Government on the Review. We will be seeking clarity and consistency of policy from the Government to support term investments in the sector, the maintenance of an open and competitive market for power generation and equality for all forms of renewable generation. In particular, we will be seeking a relaxation of the 10% cap on co-fired biomass ROCs which presently becomes effective on 1 April 2006.

LARGE COMBUSTION PLANT DIRECTIVE

On 3 February 2006, under LCPD regulations, approximately 20GW of UK coal plant "opted in" with a further 13GW "opted out". Those opted in will be required to comply with the emissions regulations set down in the LCPD. Those opted out are limited to 20,000 operating hours post 2007. Drax "opted in" under the National Emissions Reduction Plan ("NERP"), the alternative being Emission Limit Values ("ELV"), on the basis that this will serve to retain the optionality and flexibility of the plant and therefore the opportunity to add value. Under NERP, coal generators are subject to annual emission limits relative to historic generation levels, whilst under ELV there is a 48 hour emission constraint.

EU EMISSIONS TRADING SCHEME

During the course of 2006, across the European Union each country's National Allocation Plan ("NAP") for Phase II of the Emissions Trading Scheme will be announced. Drax is active in the UK Government's consultation process on the UK Phase II NAP.

Outlook

The Refinancing of the Group together with the Listing on 15 December 2005 transformed the capital structure of Drax. The new capital structure enables us to align the operational, trading and financial strategies of the business to deliver greater shareholder value. The focus going forward is to deliver this value.

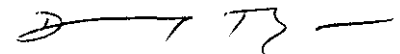
Key to the success of the delivery will be the sustained performance of the Drax team to improve on the good results achieved in 2005. We will continue to invest in the development of our staff with a keen focus on the performance culture that is now well established.

Within the business work will continue on improving plant performance and seeking areas to enhance the business by further developing fuel and product optionality. There are a number of EBITDA enhancement projects which we identified in 2005 which we will aim to deliver in 2006 and 2007. In addition, the improvement in credit status has significantly enhanced our ability to trade in the power, coal and carbon markets. It has provided access to greater depth and tenor in all of these markets. Our strategy is to extend our forward contracts whilst retaining a significant exposure to the commodity markets in order to exploit the full value of the optionality of the power plant and the expertise of the Drax trading team.

As at 3 March 2006, Drax had contracted 75% of expected 2006 output at an average price of £46.9/MWh, and 47% of expected 2007 output at an average price of £49.2/MWh. Corresponding fixed price coal and carbon have been secured to underpin these sales. Overall our volume of forward power sales has grown by over 49% in the 11 weeks from 15 December 2005 to 3 March 2006 reflecting both our increased credit capacity and counterparty interest.

Given current trading expectations and the continued development of our hedge position coupled with effective cash management, we expect during 2006 to start to deliver on our commitment to return surplus cash to our shareholders.

We will remain active in the regulatory debate. We believe coal is critical to the UK energy mix going forward if the Government is to achieve its objectives of delivering security of supply, affordability and tackling climate change where burning biomass with coal has much to contribute. We will be seeking clarity, coherence and consistency of Government policy and an equal treatment of biomass co-fired generation with other renewable energy.



Dorothy Thompson
Chief Executive
7 March 2006

- **generation and trading** The principal activity of Drax is the operation of the Power Station and the trading of the electricity it produces. All electricity is sold in the wholesale market, through the balancing mechanism or used by the Power Station.

Operating and Financial Review

Overview

Drax Group plc was introduced to the Official List of the UK Listing Authority and its ordinary shares commenced trading on the London Stock Exchange on 15 December 2005. Drax Group plc is the ultimate holding company of Drax Power Limited, the owner of Drax Power Station.

The principal activity of Drax is the operation of the power station and the trading of the electricity it produces. Drax is the largest coal-fired power station in the UK, with a nominal capacity of 3,960MW and a registered generating capacity of 3,870MW. All electricity generated is sold in the wholesale market, through the balancing mechanism or used by the power station. Fuel is purchased from a variety of UK and international sources. CO₂ emissions allowances required by the Group in excess of its allocation under the UK National Allocation Plan (the "UK NAP") are also purchased from a variety of UK and international sources.

For the year ended 31 December 2005, Drax produced an EBITDA of £239m and an operating profit of £354m (including exceptional items and unrealised losses on derivative contracts which together improved operating profit by £146m). For the year ended 31 December 2004, EBITDA was £90m and operating profit was £55m.

Results of Operations

Drax Group's revenues from generation during the year ended 31 December 2005 were £849m, compared to £549m during the corresponding period in 2004, an increase of £300m (or 55%). This increase was mainly due to increases in average electricity capture prices over the period. Power sold in the year ended 31 December 2005 was 23.2TWh, compared to 22.9TWh in the corresponding period in 2004. Included within revenues from generation are revenues from the sale of by-products (ash and gypsum), the provision of ancillary services, the sale of ROCs, LECs and SO₂ emissions allowances. In 2005 these revenues totalled £32m compared with £26m in 2004.

Drax purchases power in the market when the cost of power in the market is below Drax's marginal costs of production in respect of power previously contracted by the Group and to cover any shortfall in generation. The cost of purchased power has remained relatively constant between each of the two years. Under IFRS, the cost of power purchased is treated as fuel costs, and revenue has been adjusted accordingly.

Year ended 31 December 2005 compared to year ended 31 December 2004

	Years ended 31 December	
	2005 £'m	2004 £'m
Revenue		
Revenue from generation	848.8	549.3
Revenue associated with power purchases	79.8	74.8
	928.6	624.1
Fuel costs⁽¹⁾		
Fuel costs in respect of generation	(459.7)	(309.9)
Costs of power purchases	(79.8)	(74.8)
	(539.5)	(384.7)
Gross margin	389.1	239.4
Other operating expenses excluding depreciation, amortisation and exceptional items ⁽²⁾	(149.7)	(151.9)
Other income	-	2.5
EBITDA⁽³⁾	239.4	90.0
Depreciation and amortisation	(31.2)	(35.0)
Other operating income – net exceptional credit	263.3	-
Unrealised losses on derivative contracts	(117.0)	-
Operating profit	354.5	55.0
Interest receivable	23.5	4.6
Interest payable and similar charges	(114.4)	(101.2)
Profit/(loss) before tax	263.6	(41.6)
Tax credit	18.8	35.1
Profit/(loss) for the period attributable to equity shareholders from continuing operations	282.4	(6.5)

(1) Fuel costs comprise the fuel costs incurred in the generation process, predominantly coal, together with oil and, since 2003, biomass costs. Since 1 January 2005, CO₂ emissions allowances costs have also become a substantial component of fuel costs. Fuel costs also include the cost of power purchased to meet power sale commitments.

(2) Other operating expenses excluding depreciation, amortisation and exceptional items principally include salaries, maintenance costs, connection charges (BSUoS, TNUoS) and business rates.

(3) EBITDA is defined as profit before interest, tax, depreciation and amortisation, exceptional items and unrealised losses on derivative contracts (as defined in IAS 39).

Drax's fuel costs in respect of generation during the year ended 31 December 2005 were £460m, compared to £310m during the comparable period in 2004, an increase of £150m (or 48%). This increase was primarily due to the cost of CO₂ emissions allowances (£87m in 2005) and an increase in the cost of coal and other fuels.

Reflecting the above factors, Drax's gross margin, being revenues less fuel costs, increased from £239m in the year ended 31 December 2004 to £389m in the year ended 31 December 2005, an increase of £150m (or 63%).

Drax's other operating expenses excluding depreciation, amortisation and exceptional items, were broadly flat at £152m in the year ended 31 December 2004 and £150m in the corresponding period in 2005.

EBITDA (defined as profit before interest, tax, depreciation, amortisation, exceptional items and unrealised losses on derivative contracts) was £239m in 2005 which was £149m higher than for 2004. The improvement in EBITDA reflected the improvement in gross margin.

Depreciation and amortisation in the year ended 31 December 2005 was £4m lower at £31m compared with the same period in 2004. The depreciation and amortisation charge for 2004 included £2m in respect of losses on disposal of property, plant and equipment.

Exceptional operating income for the year ended 31 December 2005 of £263m, comprised credits of £19m due to the reversal of provisions relating to impairment of tangible fixed assets and £311m as a result of three distributions received by Drax under the TXU Claim. These items were partially offset by a charge for cash and share-based payment transactions under the Drax Group Limited Long-Term Incentive Plan ("LTIP") of £38m, as well as costs incurred with respect to the Refinancing and Listing of £29m. Additional information relating to these exceptional items is included in the Notes to the Consolidated Financial Statements. Drax had no exceptional operating income or expenses in the year ended 31 December 2004.

£33.9/MWh

- Average capture price increased by 51% on 2004

IAS 32 and IAS 39, the International Financial Reporting Standards in respect of derivatives and financial instruments, are applicable to Drax for the period from 1 January 2005. As a result of applying these standards, unrealised losses of £22.3m and unrealised gains of £8m on derivative contracts were recognised within liabilities and assets respectively at 31 December 2005 (as compared to unrealised losses of £20m and unrealised gains of £15m at 1 January 2005). The unrealised losses principally relate to the mark-to-market of Drax's forward contracts for power yet to be delivered and some coal contracts, which meet the definition of derivatives under IAS 39. The out-of-the-money position mainly reflects prices in Drax's forward sales contracts for power against rising market prices for power.

For the period from 1 January 2005 to 30 June 2005, mark-to-market movements on these contracts were reflected directly in the income statement, as appropriate hedge accounting documentation had not been put in place. This resulted in an expense of £117m relating to unrealised losses on derivative contracts being recognised in the income statement for 2005.

For the purposes of IAS 39, from 1 July 2005, the Group has put in place appropriate hedge accounting documentation to enable it to achieve hedge accounting for a large proportion of its commodity contracts. As a result, mark-to-market movements on contracts which are now considered to be effective hedges are recognised through the hedge reserve in the balance sheet.

Reflecting the above factors, Drax's operating profit increased from £55m in the year ended 31 December 2004 to £354m in the year ended 31 December 2005, an increase of £299m. Operating profit for 2005 includes exceptional operating income of £263m and unrealised losses on derivative contracts of £117m as described above.

Interest payable and similar charges in the year ended 31 December 2005 were £114m, compared to £101m in the same period in 2004, an increase of £13m (or 13%). The increase reflects a reduction in interest payable on borrowings, principally as a result of repayments of the Group's B Debt prior to 15 December 2005 following receipts under the TXU Claim, offset by a charge of £23m resulting from the termination of interest rate swap contracts on Refinancing and Listing.

Interest receivable of £24m in the year ended 31 December 2005 includes a credit of £18m in respect of previously recognised unrealised losses on terminated swap contracts, accounted for under IAS 39 from 1 January 2005.

Drax's tax credit during the year ended 31 December 2005 was £19m, compared to a tax credit of £35m for the comparable period in 2004. The tax credit in 2005 reflects the utilisation of tax losses brought forward from earlier years, which more than offsets the profit before tax for the year. The tax credit for 2004 reflects the loss for the year and the tax effect of the financing structure.

Reflecting the above factors, Drax had a profit for the year from continuing operations of £282m in the year ended 31 December 2005, compared to a loss of £7m in the year ended 31 December 2004.

Key Factors Affecting the Business

The profitability of Drax is determined by certain primary drivers: the difference between the price of electricity available in the market and the cost of generation; and the availability of the six independent generating units which comprise the power station. The cost of generation includes the cost of coal (or other fuel), the cost of CO₂ emissions allowances, and operating and maintenance costs.

During the period under review, the Group's financial condition and results of operations were significantly impacted by a financial restructuring effective on 15 December 2005 (the "Refinancing and Listing") and receipt of distributions from the Administrators of TXU Europe Energy Trading Limited and TXU Europe Group plc.

PRICE OF ELECTRICITY

The price that Drax realises when it sells electricity is critical to its results from operations. Drax sells all of the electricity it generates into the physical power market for Great Britain. Drax trades mainly in the wholesale market, through a mixture of deals consistent with Drax's hedging strategy, including medium-term bilateral power sales (6–12 months), structured deals and short-term deals. The hedging strategy recognises market limitations, alongside balance of certainty and returns.

The table below illustrates the average capture price Drax realised on a calendar year basis together with the market closing price for each season:

	Years ended 31 December	
	2005	2004
Average capture price (£/MWh) ⁽¹⁾	33.9	22.5
	2005	2004
Summer market close (£/MWh)	29.0	18.5
	2005/ 2006	2004/ 2005
Winter market close (£/MWh)	49.2	36.7

(1) Capture price is the average price achieved for power sold.

Electricity prices are volatile, for example the wholesale electricity price for power to be delivered in Winter 2005/06 ranged from £18.1/MWh in April 2002 to £67.0/MWh in July 2005, driven principally by increases in fuel costs for gas-fired generators, a narrowing of the UK's generation margin and upward pressure from the introduction of the EU Emissions Trading Scheme (the "EU ETS") in January 2005, which requires that fossil fuelled generators purchase sufficient CO₂ emissions allowances to meet any excess over their allocation under the UK NAP.

Drax's average capture price rose from £22.5/MWh for the year ended 31 December 2004 to £33.9/MWh for the year ended 31 December 2005. The forward base load power prices for Summer 2006, Winter 2006/07 and Summer 2007 were approximately £42.1/MWh, £59.7/MWh and £42.9/MWh respectively as at 3 March 2006. Peak and extended peak prices are generally significantly higher than baseload prices in the UK market, whilst off-peak prices are generally significantly lower.

PRICE OF COAL

Coal costs make up the majority of Drax's fuel costs and significantly impact its results from operations. Drax burnt approximately 9.3 million tonnes of coal in 2005 and approximately 9.2 million tonnes in 2004, purchased from a variety of domestic and international sources on either fixed or variable priced contracts with different maturities. Currently the mix is broadly as follows: 4 million tonnes from UK Coal Mining Limited ("UK Coal"), 1.5 to 2 million tonnes of Scottish coal and 3.5 to 4 million tonnes from international suppliers.

Drax burnt 9.3 million tonnes of coal in 2005, purchased from a variety of domestic and international sources.

Drax experiences less volatility in the UK coal market than in the power market as Drax typically enters into long-term supply contracts with UK suppliers, including UK Coal, and can leverage its buying power. Internationally sourced coal comes from a variety of countries including Russia, South Africa and Colombia and requires shipping, port and rail transport. Spot prices for internationally traded coal delivered into North-West Europe (as reflected by the TFS API 2 index) are volatile. For example, prices per tonne rose from US\$65 at the end of March 2004 to US\$79 at the end of June 2004, but had fallen back to US\$54 at the end of December 2005.

A five-year fixed price supply contract with UK Coal, the First Coal Supply Agreement, expires on 31 March 2006. Drax signed heads of terms on 16 July 2004 for a Second Coal Supply Agreement, a five-year, semi-fixed price contract effective from January 2005 to December 2009 for 500,000 tonnes in 2005 and 3 to 4 million tonnes per annum thereafter, to run concurrently with the First Coal Supply Agreement until its expiry on 31 March 2006.

A dispute arose between Drax and UK Coal concerning its difficulties in satisfying the terms of the First Coal Supply Agreement, which was subsequently settled on 11 August 2005 by way of an amendment agreement. The terms of the amendment include that UK Coal will deliver any shortfalls in supply of coal to Drax under either the First or Second Coal Supply Agreement by certain agreed dates at agreed prices, which are below the international coal price.

OUTAGES AND PLANT UTILISATION LEVELS

The maximum theoretical amount of electricity that Drax can sell is directly related to the output of the plant; the principal limitation to the plant's output is the number and duration of outages.

Electrical output is measured by means of reference to the load factor of the power station, which is the ratio of the actual output to the maximum possible output over a period of time. In general, the plant will generate if available and if the market price for electricity in the running period is greater than the marginal cost of production. Thus, the load factor of the plant will be constrained by plant availability (for example, there would be lower availability if there were higher plant forced outages) and marginal costs of generation compared with market prices for electricity.

The following table illustrates Drax's load factor and electrical output for 2005 and 2004:

		Years ended 31 December	
		2005	2004
Load factor ⁽¹⁾	%	73.9	69.1
Electrical output (net sales)	TWh	23.2	22.9

(1) The load factor for 2005 represents gross merchant sales before net power purchases in the balancing mechanism divided by the maximum theoretical generation of the plant. The load factor for 2004 represents gross merchant sales after net power purchases in the balancing mechanism divided by the maximum theoretical generation of the plant. The load factor for 2005 after net power purchases was 70.1%.

The forced outage rate relates to the time taken to repair equipment failures which have caused loss of availability or a decrease in output of a process plant item. The planned outage rate covers planned events for outages and major repairs and renewals.

The following table illustrates Drax's outage rates and availability for 2005 and 2004:

		Years ended 31 December	
		2005	2004
Planned outage rate ⁽¹⁾	%	7.1	7.8
Forced outage rate ⁽²⁾	%	6.1	11.8
Total outage rate	%	12.8	18.7
Availability	%	87.2	81.3

(1) The planned outage rate is expressed as a percentage of registered capacity. Therefore, the aggregate of the forced outage rate and planned outage rate will not equate to the total outage rate.

(2) The forced outage rate is expressed as a percentage of planned capacity available (that is, this includes a reduction for planned losses).

Drax's maintenance regime includes a major planned outage for each unit every four years. Consequently, there is an irregular pattern of planned outages and associated expenditure, since in two of the four years, two units will undergo a major outage. During 2005, although interim header replacement outages on two units were completed ten days ahead of schedule, the major planned outage on unit 6 overran by 17 days due to bearing failures on start-up. 2004 included two major planned outages.

The lost generation opportunity in 2005 from forced outages was 1.9TWh, compared to 3.6TWh in 2004, resulting in a forced outage rate of 6.1%

compared to 11.8% in 2004. Management have targeted further improvements in forced outage rates by focusing on preventing minor predictable failures and seeking to avoid major failures using historical Drax operating data together with original equipment manufacturer and industry experience. In 2005, progress was made in both areas with minor predictable failures falling from 6.7% in 2004 to 5.2% and major failures from 5.1% to 0.9%. Drax management believe further progress can be made and will continue the programmes initiated at the end of 2004. These programmes include: improved inspection and equipment monitoring; better quality repairs; equipment upgrades; and the improved provision of critical spares. In addition, Drax aims to achieve stable operations through improved maintenance practices and by seeking whenever possible to reduce the amount of operating unit thermal cycling. Tube leaks have historically been the single largest source of forced outages. In 2005 there were 20 tube leaks, compared to an average of 38 for each of the five years 2000 to 2004. The 2005 tube leak performance was the best the station has ever achieved.

INTRODUCTION OF EU EMISSIONS TRADING SCHEME

Under the EU ETS, which came into effect on 1 January 2005, companies are free to buy and sell CO₂ emissions allowances which have been allocated to the installations covered by the scheme. Drax has been allocated (at no cost) 43,662,561 tonnes of CO₂ emissions allowances (equivalent to approximately 14.55 million tonnes per annum) under the UK NAP for Phase I of the scheme (2005–2007). This CO₂ emissions allowances allocation is equivalent to the amount of CO₂ that the Power Station would be expected to emit in order to sell approximately 16.1TWh of electricity per annum. For generation above this level, Drax needs to purchase further CO₂ emissions allowances in the market, save to the extent that it is able to increase the proportion of biomass (deemed to be carbon free for the purposes of the EU ETS) in its fuel mix.

Drax has put in place certain contracts to purchase additional CO₂ emissions allowances and expects to purchase further CO₂ emissions allowances in the market. The Group will, therefore, incur additional costs to the extent that the plant generates in excess of the level of generation supported by Drax's allocation of CO₂ emissions allowances under the UK NAP (16.1TWh per annum), and this will have a direct bearing on Drax's costs of operation.

£311m

o Receipts from the TXU Claim (net)

During the year ended 31 December 2005, the price for CO₂ emissions allowances was volatile, with a low of €7/tonne and a high of more than €25/tonne. The significant rise in CO₂ emissions allowances prices since the introduction of the EU ETS has, in part, been linked to record high oil, gas and power prices in Europe which has resulted in the increased use of fuels such as coal in European power generation.

Drax's CO₂ emissions allowances requirement for the year ended 31 December 2005, in excess of those allocated under the UK NAP, was approximately 6.3 million tonnes, based on CO₂ emissions for 2005 estimated at 20.9 million tonnes and on net generation of approximately 23.2TWh. As at 31 December 2005, 6.3 million tonnes had been acquired at an average cost of £13.79/tonne via a number of CO₂ emissions allowances purchases, and structured deals which include the provision of CO₂ emissions allowances as part of the transaction.

The market for CO₂ emissions allowance trading is relatively new, and therefore Drax, like all companies affected by EU ETS, is continuing to develop its knowledge of this market. Currently, Drax has a policy of generally ensuring its electricity sales are matched with sufficient CO₂ emissions allowances. Drax expects to participate more actively in the CO₂ market as it develops and this may provide opportunities to add value to Drax's business.

REFINANCING AND LISTING

The Refinancing and Listing took place on 15 December 2005, resulting in the creation of a new holding company, Drax Group plc. Pursuant to the schemes of arrangement under which the Refinancing and Listing was implemented, the existing debt of the Group was settled, partially through the issue of new debt, and partially through the issue of ordinary shares in Drax Group plc. Also on 15 December 2005, Drax Group plc was introduced to the Official List of the UK Listing Authority and its ordinary shares commenced trading on the London Stock Exchange.

The Refinancing and Listing involved a cash payment of £112m to A2 Debt holders in respect of an equal amount of A2 Debt, and an exchange of the balance of A2 and A3 Debt of £433m for new ordinary shares in Drax Group plc. In addition, the existing ordinary shares of Drax Group Limited, the previous holding company, were exchanged for new ordinary shares in Drax Group plc. The outstanding A1 Debt of £388m and B Debt of £82m was repaid at par, and previously deferred interest on B Debt and accrued interest on each of the tranches of debt of £63m was repaid in full. Interest rate swap contracts with a notional value of £400m, principally related to the A1 Debt, were also cancelled, resulting in a termination payment of £23m.

The new ordinary shares in Drax Group plc issued to A2/A3 Debt holders and existing shareholders of Drax Group Limited were issued by way of schemes of arrangement, and therefore did not constitute an offer of securities to the public. Consequently, Listing took place by way of an introduction.

At the same time, the Group entered into new debt facilities, which included a Term loan of £500m and a Bridge loan of £77m, as well as a letter of credit facility of £200m and a revolving credit facility of £100m. The Term loan is subject to a fixed amortisation profile beginning on 30 June 2006 and ending on 31 December 2010. The Bridge loan has first priority over the TXU claim and the proceeds thereof.

The total costs of the Refinancing and Listing amounted to £45m, of which £29m has been included within exceptional other operating expenses in the income statement. The remaining amount of £16m has been deducted from debt and is being amortised to interest payable over the duration of the Group's new debt facilities.

TXU CLAIM

In 1999, whilst owned by AES Corporation, Drax entered into the TXU Hedging Contract, a 15-year power purchase agreement with TXU Europe Energy Trading Limited ("TXU"). TXU defaulted on the contract in 2002, and together with certain other members of the TXU Group, filed for administration in the UK. On terminating the contract, Drax issued a claim (the "TXU Claim"), ultimately agreed by the Administrators of TXU at approximately £348m (including VAT), in respect of unpaid power purchased by TXU and liquidated damages for default under the contract.

On 30 March 2005, the Group received a first distribution of £205m (net of VAT and a payment by the Group to TXU Europe Limited) under the TXU Claim. This amount was subsequently paid to B Debt holders on 15 April 2005. On 2 August 2005, the Group received a second distribution of £51m (net of VAT) under the TXU Claim. This amount was subsequently paid to B Debt holders on 17 August 2005.

On 19 January 2006, the Group received a third distribution of £55m (net of VAT) under the TXU Claim. The third distribution has been recognised in the income statement for the year ended 31 December 2005, and together with the first and second distributions, resulted in exceptional operating income of £311m for the year. The third distribution is included as a receivable balance at 31 December 2005 and was used to make a prepayment of the Group's Bridge loan facility on 23 January 2006.

At the time of approving the financial statements the Group had a further £26m (including VAT) outstanding under the TXU Claim. The directors have reasonable expectations that the Group will receive repayment of this amount broadly in full by early 2007.

Liquidity and Capital Resources

Net debt reduced to £462m in 2005 from £1,208m in 2004. The main reasons for the reduction were the improvement in gross margin, receipt of distributions from the TXU Claim and the exchange of debt for equity as part of the Refinancing and Listing.

£500m

• Five year amortising Term loan facility

£200m

• Letter of credit facility

£77m

• Bridge loan facility

£100m

• Revolving credit facility

Cash and cash equivalents stood at £88m on 31 December 2005 compared with £38m on 31 December 2004. The increase in cash and cash equivalents is analysed in the table below:

ANALYSIS OF CASH FLOWS

	Years ended 31 December	
	2005 £'m	2004 £'m
Net cash generated from operating activities	348.5	17.1
Net cash used in investing activities	(25.0)	(13.7)
Net cash (used in)/generated from financing activities	(273.2)	0.5
Net increase in cash and cash equivalents⁽¹⁾	50.3	3.9

(1) For the purposes of the cash flow statements, cash and cash equivalents exclude amounts held in escrow as at 31 December 2005 and in debt service reserve accounts as at 31 December 2004. The movements in these accounts are included as a component of net cash generated from operating activities.

Net cash generated from operating activities was £349m in the year ended 31 December 2005, compared to £17m for the corresponding period in 2004, an increase of £332m. The increase includes the first and second distributions received in 2005 under the TXU Claim of £256m, as well as the impact of improved business performance, gross margin having increased by £150m in 2005. These items were partially offset by an increase in interest paid of £66m, which includes payment of previously deferred interest of £25m as well as £23m related to the termination of interest rate swap contracts on Refinancing and Listing.

Net cash used in investing activities was £25m in the year ended 31 December 2005, compared to £14m for the corresponding period in 2004. This reflected higher levels of capital expenditure in 2005.

Net cash used in financing activities was £273m in the year ended 31 December 2005, compared to net cash generated from financing activities for the corresponding period in 2004 of £0.5m. 2005 includes repayment of borrowings prior to the Refinancing and Listing of £268m, which comprises repayment of B Debt of £256m funded out of the first and second distributions under the TXU Claim, as well as a prepayment of £12m of A1 Debt on

30 June 2005. Also included in 2005 is repayment of borrowings on Refinancing and Listing of £583m, which comprises A1 and B Debt repayment at par of £388m and £82m respectively, as well as A2 cash consideration of £112m. These debt repayments were partially met by new debt issued on Refinancing and Listing of £577m.

Reflecting the above factors, cash and cash equivalents increased by £50m in the year ended 31 December 2005, compared to £4m for the corresponding period in 2004. Cash and cash equivalents were £88m at 31 December 2005, compared to £38m at 31 December 2004. Drax's policy is to invest available cash in short-term bank deposits.

CAPITAL RESOURCES

On 15 December 2005, the Group's existing debt was replaced by new debt facilities comprising a £500m five year amortising Term loan facility, a £200m letter of credit facility, a £100m revolving credit facility, and a £77m Bridge loan facility. The Term loan facility is secured on a pari passu basis with the letter of credit facility and the revolving credit facility and any other permitted secured indebtedness. The Group's debt is guaranteed and secured directly by each of the principal subsidiaries of the Company and also by the Company. Standard & Poor's Ratings Group ("S&P") assigned a BBB senior secured debt rating with a recovery rating of "1" to the Term loan facility, the letter of credit facility and the revolving credit facility. Drax is required to fund a debt service reserve account if it does not meet the specified historic annual debt service cover ratio on any of the six-monthly calculation dates, with the first calculation date being on 31 December 2006.

The letter of credit facility can be used to provide letters of credit to counterparties or exchanges in relation to Drax's trading business. The final maturity date of the letter of credit facility is 15 December 2012. The Group guarantees the obligations of a number of banks in respect of the letters of credit issued by those banks to counterparties of the Group. As at 31 December 2005 the Group's contingent liability in respect of these guarantees amounted to £77m (2004: £27m).

The revolving credit facility can be used to finance working capital requirements. It may also be used to provide letters of credit up to a maximum of £100m or provide cash collateral, to the extent that counterparties do not accept letters of credit, up to a maximum of £20m. The final maturity date is 15 December 2010.

The Bridge loan facility must be repaid in full by 31 December 2008. Proceeds under the TXU Claim must be applied to repay the Bridge loan facility. Following a third distribution under the TXU Claim on 19 January 2006, £55m of the Bridge loan was repaid on 23 January 2006 leaving a balance of £22m outstanding. The third distribution has been recognised in the income statement for the year ended 31 December 2005 and has been included as a receivable balance at 31 December 2005. The debt which was repaid on 23 January 2006 has been shown as repayable within one year at 31 December 2005.

Under the new debt facilities, the Group can incur further financial indebtedness up to an aggregate of £100m so long as S&P provides written confirmation that the Term loan facility will maintain an investment grade credit rating of at least BBB- following the incurrence of the further secured indebtedness. In addition, Drax can enter into additional finance leases up to an aggregate value of £10m. The Group can also incur overdraft and other short-term borrowings or facilities not to exceed £15m and subject to certain other restrictions. The new debt facilities may be prepaid without penalty.

SEASONALITY OF BORROWING

Drax faces seasonality in its business with higher demand in the Winter period and lower demand in the Summer months. Accordingly, cash flow during the Summer period is materially reduced due to the combined effect of lower prices and output, while maintenance expenditures are increased during this period due to planned outages. The £100m revolving credit facility will assist the Group in managing the cash low points in the cycle, where required.

CONTRACTUAL COMMITMENTS

The following table illustrates Drax's contractual obligations, excluding interest, as they fall due as at 31 December 2005:

Capital expenditure in 2005 was in support of fuel diversification, environmental compliance and meeting improved reliability and safety targets.

	Payments due by period				
	Total £'m	2006 £'m	2007 £'m	2008 £'m	2009-2015 £'m
Debt	577.0	105.1	35.0	51.9	385.0
Coal purchases	736.6	289.8	215.7	126.1	105.0
Contracted capital expenditure	191	9.7	3.5	5.9	-
Support contract payments	25.3	18.1	4.8	1.1	1.3
Total	1,358.0	422.7	259.0	185.0	491.3

CAPITAL EXPENDITURE

	Payments due by period		
	2004 £'m	2005 ⁽¹⁾ £'m	2006 £'m
Low NO _x retrofit equipment	4.2	3.7	7.0
Process control system refurbishment project	-	6.5	4.5
Boiler efficiency	1.4	-	-
Biomass handling and storage	-	3.1	3.5
Plant spares	1.8	1.4	1.4
Strategic spares	-	3.9	2.0
Other	6.3	6.5	11.5
Total	13.7	25.1	29.9

(1) Capital expenditure for 2005 excludes an accounting adjustment of £1.9m in relation to the estimated decommissioning, demolition and site remediation costs at the end of the useful economic life of the Group's generating assets on a discounted basis.

Capital expenditure was £25m in 2005 compared with £14m in 2004. The increase in capital expenditure in 2005 was in support of fuel diversification (biomass and petcoke), environmental compliance and meeting improved reliability and safety targets.

Drax expects to incur capital expenditure of approximately £100m in the plant over the next three years in support of current operations. The investment programme beyond 2008 is expected to be more in line with 2004 levels where the annual spend on capital expenditure was approximately £14m, although it is expected that additional expenditure will be incurred ahead of the requirements of the Large Combustion Plant Directive from 2016. The higher capital expenditure programme includes investment in low NO_x retrofit equipment such as Boosted Over Fire Air ("BOFA") systems (£7m in 2006) and the completion of the upgrade of unit control systems (£5m in 2006). Drax also intends to evaluate other opportunities which may result in additional expenditure. Drax expects to fund future capital expenditure from cash from continuing operations.

The above table illustrates both past and projected capital expenditure for the years indicated. The projections reflect various estimates and assumptions by management relating to the implementation of the business strategy, which may not be accurate, may not be realised, and are inherently subject to uncertainties that are difficult to predict and may be beyond Drax's control.

OFF-BALANCE SHEET ARRANGEMENTS

Other than the letters of credit referred to above, no member of the Group has entered into any transactions with unconsolidated entities concerning financial guarantees, subordinated retained interests, derivative instruments or other contingent arrangements that expose Drax to material continuing risks, contingent liabilities, or any other obligation under a variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to Drax.

Critical Accounting Policies

Note 3(D) to Drax's Consolidated Financial Statements on page 48 of this Annual Report includes a summary of the significant accounting principles and policies used in the preparation of Drax Group plc's financial statements. The preparation of financial statements, in conformity with generally accepted IFRS accounting principles, requires management to make estimates and assumptions that affect the amounts reported in the financial statements and notes to the financial statements. Actual results could differ from these estimates. Certain accounting policies have been identified as the most critical accounting policies by considering which policies involve particularly complex or subjective decisions or assessments and these are discussed below:

FIXED ASSETS AND DEPRECIATION

Estimated remaining useful lives and residual values are reviewed annually, taking into account prices prevailing at each balance sheet date. The carrying values of fixed assets are also reviewed for impairment where there has been a trigger event 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 the directors' reasonable estimates of future prices, output and costs and is, therefore, subjective.

PENSIONS

Within the UK, Drax operates an approved defined benefit scheme. Drax accounts for this scheme in accordance with IAS 19 "Employee Benefits" with the cost of providing benefits determined using the projected unit credit method, and actuarial valuations being carried out at each balance sheet date. Inherent in these valuations are key assumptions, including discount rates, expected returns on plan assets, and salary and pension increases. These actuarial assumptions are reviewed annually and modified as appropriate. Drax believes that the assumptions utilised in recording 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.

Drax manages the commercial risks faced by the Group in accordance with policies approved by the Board.

EMISSIONS ALLOWANCES

Liabilities in respect of obligations to deliver emissions allowances are recognised as incurred by reference to generation for the period. Any liabilities recognised are measured based on the current estimates of the amounts that will be required to satisfy the net obligation, taking into account the market price of emissions allowances at the balance sheet date. The actual cost of those allowances not already acquired may be different and the number of allowances may be different as actual generation may not be the same as expected generation.

DEFERRED TAXATION

Full provision is made for deferred taxation, as required under IAS 12 "Income Taxes", at the rates of tax prevailing at the period end dates unless future rates have been substantively enacted. Deferred tax assets are recognised where it is more likely than not that they will be recovered.

DERIVATIVES

Drax has applied IAS 32 "Financial Instruments: Presentation and Disclosure" and IAS 39 "Financial Instruments: Recognition and Measurement" from 1 January 2005. IAS 39 requires derivative financial instruments to be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in earnings unless specific hedge accounting criteria are met. The fair values of derivative instruments for commodities are determined using forward price curves. Forward price curves represent Drax's estimates of the prices at which a buyer or seller could contract today for delivery or settlement of a commodity at future dates. Drax generally bases its forward price curves upon readily obtainable market price quotations, as Drax's commodity 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.

Market Risks and Treasury Policies

Drax manages the commercial risks faced by the Group in accordance with policies approved by the Board.

COMMODITY RISK

Drax is exposed to the effect of fluctuations in commodity prices, particularly the price of electricity, which is the commodity produced by Drax, in addition to the price of coal (and other fuels), which is essential to the production of electricity, and since 1 January 2005, the price of CO₂ emissions allowances. Price variations and market cycles have historically influenced Drax's financial results and are expected to continue to do so.

Drax has a policy of making forward sales of power when profitable compared with marginal costs of fuel and CO₂ emissions allowances.

Drax purchases coal on either fixed or variable priced contracts with different maturities from a variety of domestic and international sources. Drax purchases CO₂ emissions allowances on fixed price contracts with different maturity dates from a variety of domestic and international sources.

COUNTERPARTY RISK

As Drax relies on third-party suppliers for the delivery of coal and other goods and services, it is exposed to the risk of non-performance by these third-party suppliers.

Drax purchases a significant majority of its coal under contracts with UK Coal. There is a risk that if UK Coal falls into financial difficulty and/or fails to deliver against the contracts, there would be additional costs associated with securing coal from other suppliers. Should UK Coal fall into administration, Drax could be subject to temporary loss of deliveries, higher coal prices and accelerated payments.

Drax enters into fixed price 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 Drax financial distress or increase the risk profile of Drax.

The investment of surplus cash is undertaken to maximise the return within Board approved policies. These policies set out minimum rating requirements, maximum investment with any one counterparty and the maturity profile.

INTEREST RATE RISK

Drax is exposed to interest rate risk principally in relation to its outstanding bank debt. In particular, it is exposed to changes in the LIBOR interest rate of sterling-denominated debt, as substantially all of its debt is both denominated in sterling and has a variable LIBOR rate. Drax partially manages this risk with interest rate hedges on a proportion of its debt facilities.

FOREIGN CURRENCY RISK

Foreign currency exchange contracts are principally entered into to hedge Drax's requirement to purchase coal from international sources in US dollars, and to purchase CO₂ emissions allowances in euros. Drax also purchases coal and CO₂ emissions allowances from a range of domestic and international suppliers.

Profit Forecast for the Year Ended 31 December 2005

The prospectus, dated 28 October 2005, prepared in connection with the Refinancing and Listing included a forecast of profit before interest, tax, depreciation and amortisation ("EBITDA"), profit before interest and tax ("operating profit"), and net profit before interest expense and tax (together "the Forecast") for the year ended 31 December 2005.

The basis of preparation and principal assumptions for the Forecast are set out on pages 154 and 155 of the prospectus. The assumptions included that the Forecast was based on average prices of electricity and coal prevailing over the five days up to and including 21 October 2005 and it was assumed that there would be no change in the future prices of electricity and coal. In addition, following the completion of a structured contract with EDF Trading Limited in October 2005, the prospectus noted that the Group had substantially fixed the cost of CO₂ emissions allowances for 2005.

The following table provides a comparison of the Forecast to the actual results for the year ended 31 December 2005 and also compares forecast and actual EBITDA excluding exceptional items and unrealised losses on derivative contracts.

"All of any remaining cash flow, subject to the availability of reserves and after debt payment and other expected business requirements, will be distributed to shareholders. A significant cash surplus is expected to arise in 2006."

£50m

o Base dividend each year

	Year ended 31 December		
	Forecast £ million	Actual £ million	Variance £ million
EBITDA – before exceptional items and unrealised losses on derivative contracts	220	239	19
Exceptional credit related to termination of TXU Contract and financial restructuring	275	330	55
LTIP expenses arising from cash and share-based payment transactions	(38)	(38)	–
Estimated fees and expenses of the Refinancing and Listing	(27)	(29)	(2)
Unrealised losses on derivative contracts	(119)	(117)	2
EBITDA – after exceptional items and unrealised losses on derivative contracts	311	385	74
Depreciation and amortisation	(32)	(31)	1
Operating profit	279	354	75
Interest income ⁽ⁱ⁾	5	6	1
Net profit before interest expense and tax	284	360	76

(i) Interest income excludes a credit of £18m included in interest receivable in respect of previously recognised unrealised losses on interest rate swap contracts terminated on Refinancing and Listing. This credit is offset by a charge of £23m included in interest payable representing the cash cost of terminating the swap contracts.

EBITDA before exceptional items and unrealised losses on derivative contracts was £19m higher than forecast largely due to an improvement of approximately £17m in gross margin, principally reflecting higher electricity prices captured for

November and December compared to market prices on 21 October 2005, and increased generation as a result of lower than forecast forced outages for the final quarter of 2005. The significant increase in EBITDA after exceptional items and unrealised losses on derivative contracts is largely due to the improvement in gross margin noted above and £55m of exceptional operating income arising from the third distribution under the TXU Claim, received on 19 January 2006. As previously noted, the third distribution has been recognised in the income statement for the year ended 31 December 2005.

Contracted Position for 2006 and 2007

As at 3 March 2006, the Group had contracted for around 75% of expected output for 2006 at an average price of £46.9/MWh and had secured around 75% of its expected 2006 CO₂ emissions allowances requirements through a combination of allowances allocated to Drax under the UK NAP, market purchases and structured contracts. Coal had been contracted at fixed prices for around 75% of expected output.

As at 3 March 2006, the Group had contracted for around 47% of expected output for 2007 at an average price of £49.2/MWh and had secured around 68% of its expected 2006 CO₂ emissions allowances requirements through a combination of allowances allocated to Drax under the UK NAP, market purchases and structured contracts. Coal had been contracted at fixed prices for around 50% of expected output.

Distribution Policy

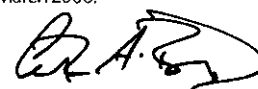
The Board has established a distribution policy which recognises Drax's exposure to commodity markets and comprises two elements.

The Board intends that Drax will pay a stable amount (£50m) by way of ordinary dividends each year (the "base dividend"). The base dividend will

comprise an interim dividend and a final dividend and it is expected that the interim dividend will represent approximately one third of the total anticipated base dividend for each year. Drax expects to pay a first interim dividend of 4 pence per share (being approximately £16.3m) for the half year ending 30 June 2006 in Autumn 2006.

In addition to the base dividend, substantially all of any remaining cash flow subject to the availability of reserves and after making provision for debt payments, debt service requirements (if any), capital expenditure, and other expected business requirements will be distributed to shareholders. A significant cash surplus is expected to arise in 2006. The amount will be dependent on a number of factors, including commodity prices and plant performance. Work has commenced to identify the most appropriate method for returning surplus cash to shareholders and it is expected that the proposed method of return will be advised at the Company's Annual General Meeting in May 2006 and that this will be followed by an indication of the likely range of distribution, timing and shareholder approval process in a Trading Update given at the end of June 2006.

This review was approved by the Board on 7 March 2006.



Gordon Boyd
Finance Director

Corporate and Social Responsibility

Overarching Corporate and Social Responsibility Policy

The Group recognises that its operations (which are all conducted by its subsidiary, Drax Power Limited) have to be conducted within a framework that reflects legislative and regulatory requirements, and is also based upon a set of voluntary policies which reflect society's expectations of a large and highly visible power station. We believe that corporate responsibility makes good business sense and we strive to balance both commercial rigours and regulatory demands of the competitive commodity market in which we operate with a commitment to our wider stakeholder group. As a responsible and responsive business with long-term ambitions, we continue to invest to comply with increasingly stringent environmental, and health and safety requirements, and communicate with the wider stakeholder group, both local and national, through being open and transparent in all that we do.

Corporate Accountability

The management and organisation of the Group is not only substantially compliant with the governance requirements of the London Stock Exchange but also sensitive to the expectations of society generally. The Board has control of the Group's policies, both in respect of its wider corporate and social responsibility, and in particular in relation to environmental, health and safety, and social issues. The Group's employees include specialists who spend all or most of their time ensuring that the Board's policies are implemented and that the established procedures for identifying and reporting on risks and opportunities and assuring compliance in these areas continue to be effective. Internal processes have been established which enable Board members and managers to review performance regularly, to set appropriate targets, and to monitor progress against them.

Interaction with Stakeholders

The Group has a wide-ranging external audience, from shareholders and lenders, through Government and the media to suppliers, non-Governmental organisations, opinion formers and the local community. We endeavour to communicate fully with each of these stakeholders through both an investor relations programme and a public affairs and community relations programme aimed at building the reputation of the Group.

INVESTOR RELATIONS

During 2005, Drax Group Limited (the holding company of the Drax group of companies until

Listing) sharpened its focus on Investor Relations and supplemented its results presentations with four investor roadshows in both the UK and US. We believe the success of the programme showed through in the 97% vote in favour of the schemes of arrangement and the consequent Listing of the Company on the London Stock Exchange.

PUBLIC AFFAIRS ACTIVITIES

Economic and environmental legislation and regulations, both national and European, have a major influence on UK electricity industry market participants. Indeed, the changes to the UK electricity market effected by legislation in the shape of the Utilities Act 2000 and the Energy Act 2004, the introduction of the New Electricity Trading Arrangements in March 2001 and the British Electricity Trading and Transmission Arrangements in April 2005, the implementation of the Renewables Obligation in April 2002, the progressive development of the EU Large Combustion Plant Directive and, at the start of 2005, the introduction of the EU Emissions Trading Scheme are examples of legislative and regulatory changes which, in a period of less than five years, have had a significant impact on the economics and dynamics of the industry.

Against this backdrop, the Group attaches importance to monitoring policy development by the UK Government and the European institutions and to analysing and assessing planned and prospective legislative and regulatory change. To help it with this task the Group has retained the services of Lord Taylor of Blackburn as Parliamentary Adviser.

During 2005, good working relations were maintained within Parliamentary and Governmental arenas, including Government officials and agents of Government. Focused briefings were used as a vehicle for raising issues of concern and presenting potential solutions to industry-wide issues. In addition, Drax took full advantage of engaging in public consultations emanating from Government departments and inquiries launched by select committees and other Government agents. During the year, two Government Ministers and the Member of Parliament for Selby, John Grogan MP, visited Drax Power Station, as did two prospective parliamentary candidates. Briefing meetings were also held in London with one further Government Minister and Government officials of both the Department of Trade and Industry, and the Department for the Environment, Food and Rural Affairs.

No political donations were made in the UK or elsewhere during 2005 and the Group's contact with those active in the political arena has been and will continue to be aimed only at the promotion of the Group's business interests. However, given the widespread doubt about the types of expenditure falling within the scope of the legislation controlling political donations, the Board wishes there to be no question of modest expenditure incidental to advocating the Group's business interests to those in government, or active in the political arena, being alleged to be in contravention of the legislation. Accordingly, shareholders will be asked to approve a resolution authorising annual expenditure up to a limit of £100,000 in respect of each of the Company and Drax Power Limited for a period of four years.

SUPPLIERS

As in previous years, we encouraged local and national companies to bid for contracts to supply the many goods and services required by the Power Station. Most of what we purchase on the contract and spares replenishment side tends to be mainly from a UK source or within the European Union. Very occasionally we go further afield. In making the various purchases, we are mindful that some companies or indeed countries may operate poor standards as far as profiteering at the expense of others, or human rights issues, are concerned. We recognise that in covering a varied marketplace, with a number of indirect manufacturers supporting the end product, it is difficult to state with some certainty that we do not trade with certain companies or countries whose standards are poor. However, we make all reasonable endeavours to ensure that we do not knowingly support or trade with such companies or countries.

COMMUNITY RELATIONS

We are committed to being a good neighbour to our local community and our "caring for the community" philosophy involves being part of local, county and business communities.

Throughout 2005, we maintained close relations with the local community through formal and informal discussions with representatives of parish, district and county councils. As a major employer, we sought to take an active role in business community organisations, such as the Selby Industrial Association and the Selby Communities and District Industrial Mission.

SPONSORSHIP

We furthered our community involvement through sponsorship activities, site visits and dedicated information. During 2005, we made charitable

A new charity initiative was launched in 2005 focusing on good safety performance during the major outage on unit 6. The Yorkshire Air Ambulance and Cancer Research UK charities both received donations.

Thousands of visitors are welcomed to the Power Station each year, last year we played host to some 3,500.

donations of £37,500 in total. Some £12,000 was donated under the direction of our Sponsorship Team across a range of community and environmental interests, and sporting activities within a 20 mile radius of the Power Station. Amongst the good causes supported were: The Green Team, a project which aims to provide a low cost practical gardening service for elderly people and people with disabilities; and Selby District Nightstop, a group devoted to tackling the problems of youth homelessness in the local district.

Sponsorship of youth sports proved popular during the year, with football, rugby and cricket clubs all benefiting. In particular, the Summer saw the launch of the Drax Village Cricket Club's youth section and we were pleased to sponsor the shirts and encourage this initiative for young people in the area.

A new initiative was launched in 2005 to focus on good safety performance during the major outage on unit 6. During the 12 week outage, £500 was donated for every seven days that went by without an accident that did not require more than first aid treatment. Employees and outage contractor, Mitsui Babcock, were each asked to nominate a charity and Cancer Research UK and the Yorkshire Air Ambulance charities each received a donation of £2,250.

Some £19,000 of the remaining donations were made through the Group's "£ for £" matching scheme, under which we match, £ for £, any monies raised for charity or good causes by employees at the Power Station. We were particularly pleased to be able to match £ for £ monies raised by one of our employees who took part in a Bikeathon to raise money for Leukaemia Research, helping him to raise the most money in the ten year history of the event.

VISITORS

Thousands of visitors are welcomed to the Power Station every year. The appeal of discovering more about how power is produced and the sheer scale of the site and its associated activities attracts schools and colleges as well as business organisations. During 2005, we hosted some 3,500 visitors which included a total of 64 schools.

Members of the public are also welcome to visit Barlow Mound, which has been developed over time through careful and imaginative management of the Barlow Mound ash disposal scheme. Formerly an old munitions site, extensive landscaping and tree planting that is now well

established has transformed this area into woodland and wetland features, picnic spots and artificial hills. This nature centre provides a complete contrast to the industrial workings of the Power Station and is specially designed to help visitors understand more about the natural habitat and ecology of the area.

Protecting the Environment

ENVIRONMENTAL POLICY

The size and characteristics of Drax Power Station mean that it has a significant impact on the environment. We recognise this and have put the management of the environment at the heart of our decision-making process. Our policy is as follows:

"Drax Power Limited recognises its responsibilities to society and the environment and is committed to being an innovative leader in the management of the environment across all its activities and in all its business decisions.

We regard compliance with legislation as a minimum level of achievement. Furthermore, we are committed to managing, monitoring and reducing, where practicable, the environmental impacts caused by our business through continual improvement of our operations, in particular emissions to air, discharges to water, disposal of waste and the use of natural resources.

We will maintain a reputation for effective environmental management, in part by certification to the international environmental management system standard, ISO 14001:1996. This system will be used to set and periodically review environmental objectives and targets.

We will discuss our activities with our stakeholders, engaging with them to help refine and broaden our understanding, taking note of their views and investigating any concerns promptly.

We will promote environmental awareness amongst our staff, business partners and contractors, ensuring that they understand the environmental aspects of their activities, that they act responsibly and are competent to carry out their jobs."

ENVIRONMENTAL MANAGEMENT SYSTEM

Drax manages its environmental compliance under an Environmental Management System ("EMS") certified to the international standard ISO 14001. Its purpose is to ensure that the Group meets its legal and policy commitments to protect and improve the environment in the course of carrying out its business.

The EMS covers all activities of the Group's operations. The Chief Executive has overall responsibility for the implementation of the EMS and for environmental compliance and performance of the business, with other staff allocated specific responsibilities as determined by the nature of the environmental impacts for which they are responsible.

The EMS contains documented procedures for each significant environmental issue and staff are trained to recognise the legal and operational requirements contained within them.

ENVIRONMENTAL COMPLIANCE

Drax operates within the conditions of its Integrated Pollution Control ("IPC") authorisation, granted by the Environment Agency and we aim to maintain compliance with no significant breaches of the regulatory limits. We recognise that emission limits will become tighter in the future and our goal is to be ahead of legal requirements for emission reductions whilst recognising the need to maintain our competitive market position.

We maintain investment in our emission abatement equipment and consider this to be a high priority. Our FGD plant already complies with known future emission limits to 2016 and we have initiated a programme of retrofitting all units with low NO_x technology (Boosted Over Fire Air technology) in order to ensure compliance with the requirements of the Large Combustion Plant Directive (LCPD) from 2008.

In addition to emissions to air, the operation of the Station results in other environmental effects, such as discharges to water, waste material production, and noise. We maintain an up-to-date understanding of the science underlying our impacts in order to contribute to the development of cost-effective control measures.

KEY ENVIRONMENTAL IMPACTS: EMISSIONS TO AIR

The principal emissions from burning coal are carbon dioxide (CO₂), hydrogen chloride (HCl), sulphur dioxide (SO₂), oxides of nitrogen (NO_x) and particulates (dust). Drax's generating units have all been retrofitted with FGD equipment and low NO_x burners to reduce emissions to the atmosphere. The FGD equipment removes, on average, at least 90% of SO₂ and HCl emissions before the flue gas is released via the chimney into the atmosphere.

	Emissions per unit of electricity generated				
	2001	2002	2003	2004	2005
Carbon dioxide (t/kWh)	0.84	0.84	0.83	0.84	0.83 ⁽¹⁾
Sulphur dioxide (10 ⁻³ t/kWh)	2.05	1.78	1.70	1.07	1.01
Oxides of nitrogen (10 ⁻³ t/kWh)	2.62	2.55	2.49	2.36	2.30
Hydrogen chloride (10 ⁻³ t/kWh)	0.18	0.16	0.03	0.03	0.01
Particulates (10 ⁻⁶ t/kWh)	13.45	15.42	11.55	16.33	18.44

(1) Accounting for the carbon free status of biomass.

KEY ENVIRONMENTAL IMPACTS:

DISCHARGES TO WATER

Procedures are in place to ensure that all discharges and drainage to water are monitored and treated where necessary to meet our discharge consent limits. There are a number of sources of discharge and drainage as part of the electricity generation process. These sources include the cooling water used to cool the condensers, which as part of the steam cycle condense steam to water after it leaves the turbines and before returning to the boilers. Cooling water is abstracted mainly from the River Ouse and boiler feedwater originates from two boreholes on site. Approximately half of the water is returned to the River Ouse at a few degrees warmer than the river water.

Also, the FGD process produces effluent water which is treated in a specially designed plant before it is discharged to the river, and there is also drainage from the main plant, coal plant and roads.

KEY ENVIRONMENTAL IMPACTS: DISPOSALS TO LAND

When coal is burnt, ash is left as a residue. The finer particles of ash, pulverised fuel ash (PFA), are collected from the flue gas by electrostatic precipitators; the heavier ash, furnace bottom ash (FBA) falls to the bottom of the boiler. The majority of ash is sold to the construction industry with the remainder sent for landfill at the Station's adjacent Barlow Mound.

Drax pays landfill tax on the PFA disposed of to the Barlow Mound. Through the Landfill Tax Credit Scheme, Drax is able to claim a tax credit against its donations to recognised Environmental Bodies. Drax has worked with Groundwork Selby since 2001 on projects designed to help mitigate the effects of landfill upon our local community. During 2005, we contributed approximately £126,000 towards seven projects, including the Selby Town Community Pond and the Airmyr Playing Fields.

Alternative Fuels

To help maintain our vital role in the UK economy and safeguard cost effective power production our fuel strategy recognises the need to sustain a ready supply of traditional quality coal and how best to incorporate alternative fuels including different fossil fuels and renewable materials. The choice of fuels has to be balanced with availability and flexibility of supply.

Through the provision of dedicated information and focused site tours we continue our policy of being open, transparent and informative about our operations. In November and December of 2005, we organised tours of the Power Station specifically for local residents to enable them to see for themselves how alternative fuels such as biomass and petroleum coke ("petcoke") are handled on site.

PETROLEUM COKE

The 18 month trial burn of petcoke from June 2005 is an integral part of our strategy of developing alternative fuels. It involves burning a blend of coal and up to 15% petcoke on one of our six generating units. Petcoke is derived from the petrochemical industry and is produced from oil.

Petcoke contains higher levels of sulphur than coal but the FGD plant at Drax ensures that, on average, at least 90% of the SO₂ is removed before gases created during combustion are emitted to the atmosphere. Thus, Drax has the capability to burn petcoke within the permitted levels already set for the Power Station by the Environment Agency.

Studies indicate that burning petcoke produces lower total emissions of trace metals (other than nickel and vanadium) and particulates than coal, boiler efficiency improves and therefore potentially less oxides of nitrogen (NO_x) gases will be produced during combustion.

There are inherent properties in petcoke that make it a beneficial fuel source, environmentally and economically. It contains roughly 30% more heat per tonne than coal, meaning that less has to be burnt to achieve the same electricity output. The amount of ash produced is considerably less, under 1% of the original weight compared with 10-18% in the case of coal, so ash disposal is significantly reduced.

With the use of petcoke we have taken our stringent monitoring procedures even further. A programme of detailed testing to measure emissions during the trial was approved by the Environment Agency, and they receive monthly reports on the results of the trial. These are also published on our website as part of our policy to be open and transparent about the trial results. In addition, we work closely with both the Environment Agency and Selby District Council to ensure that the impact of the coal/petcoke trial is fully understood.

The six months of independent testing and measurement prior to the start of the trial has shown extremely low ambient levels of both nickel and vanadium in the locality surrounding the Power Station. These data reflect regional effects rather than effects from the power stations in the area and the levels are well below safety limits set by the Environment Agency. This monitoring will run continuously during the trial.

BIOMASS

We are aware of the requirements to reduce CO₂ emissions, and we have continued to identify and use, where commercially viable, CO₂-neutral fuels, such as renewable biomass materials, to replace fossil fuels, such as heavy fuel oil and coal. In 2005, a CO₂ saving of over 450,000 tonnes was achieved through our biomass activities.

Tall oil, an oil which is derived from wood pulp, is an environmentally-friendly substitute for heavy fuel oil and marks an important development in establishing the effective use of alternative renewable fuels. Tall oil replaces heavy grade fuel oil and is burnt during a number of processes at the Power Station, for example, during the start-up cycle for each of the boilers.

We were the first power station in the UK to use tall oil, which made an important contribution to reducing our emissions during 2005. Around half of the CO₂ savings made came from burning tall oil, and emissions of SO₂ were also reduced. We will continue to burn tall oil when commercially viable.

Over the last two years we have also developed the capability to co-fire solid biomass materials with coal. Trials on a variety of biomass materials were conducted throughout the year, with the emphasis on developing the capability to burn wood and other energy crops.

We are able to add biomass to the coal before the coal is pulverised into a fine powder in the pulverising fuel mills, a process known as "through the mill". This operation has worked well during 2005, although there are limits to the amount of biomass that can be successfully blended with the coal in this way.

During the second half of 2005 a "direct injection" system was commissioned on one unit allowing greater and more reliable throughput of biomass materials.

39%

Reduction in total recordable injury rate

By the end of 2005, biomass was being co-fired at the equivalent rate of 250,000 tonnes per year.

By the end of the year, biomass was being co-fired through both "direct injection" and "through the mill" systems at the equivalent rate of 250,000 tonnes per year.

Looking ahead, we are developing a long-term strategy involving energy crops in partnership with local farmers which has the potential to significantly reduce CO₂ emissions from the Station and make a valuable contribution to the Government's target for 2010 of 10% of electricity supplied coming from renewable fuels.

Health and Safety

Health and safety is at the heart of Drax's corporate responsibility and protecting our employees and contractors from ill-health or injury and promoting employee well-being is fundamental to our business philosophy. We are committed to developing and maintaining a positive health and safety culture in which statutory requirements are viewed as a minimum standard and "world class" performance our goal.

Personal safety statistics	2005	2004
Fatality	0	0
Lost time accident	7	8
Restricted work accident	4	6
Medical treatment accident	1	5
First aid	140	182
RIDDOR ⁽¹⁾ reportable	6	6

(1) Reporting of Injuries, Diseases and Dangerous Occurrences Regulations.

Accident frequency rates ⁽¹⁾	2005	2004
Lost Time Accident Rate (LTAR)	0.35	0.42
Total Recordable Injury Rate (TRIR)	0.60	0.99
All Injury Rate (AIR)	7.16	9.67

(1) Frequency rates are calculated on the following basis (number of accidents x 100,000)/hours worked.

The total recordable injury rate dropped from 0.99 in 2004 to 0.6 in 2005, a 39% reduction. This improvement has been delivered through visible leadership, simple systems and clear expectations. These three core objectives will continue to fuel our drive for "world class" safety performance.

The new incident investigation and review process launched in 2004 continues to provide a firm platform for the identification of health and safety learning opportunities. The weekly Safety Bulletin briefing process provides a fast track for safety communication to all staff.

The safety representatives and management team members of the Health and Safety Advisory Committee (HESAC) continue to play a vital role through facilitating staff consultation on health and safety issues.

The twinning arrangement between Drax and ScottishPower's Longannet Power Station continues to produce real safety benefits for both parties. In an effort to accelerate the improvement of our safety performance, exchange visits have recently taken place with EON's Ratcliffe-on-Soar Power Station and Corus.

"Spotlight on Safety" is the Group's implementation of the internationally proven DuPont™ STOP™ programme. This behavioural safety programme, introduced in November 2004, will continue as the main vehicle for safety improvement over the next two to three years.

Employment culture

We have established a performance culture work ethic, where staff feel valued and want to come to work and perform for the good of the business. We are working towards an industrial relations climate at Drax Power that is positive, with employment policies which respect human rights and equal opportunities as well as facilitating training to develop staff and enhance competence. The Group is committed to the principles of fairness and dignity at work.

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicants concerned. In the event of a member of staff becoming disabled, every effort is made to ensure that their employment 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, as far as possible, be identical to that of other employees.

RECRUITMENT

Our apprenticeship programme was re-introduced in September 2003 amidst a growing realisation of a potential future shortfall in skilled workers, particularly in the more traditional craft disciplines. With the long-term future of the business in mind, we decided to take steps to secure the right level of human resource and the programme now forms a major component of our policy of investing in our staff. This practice was continued in 2004 and again in 2005, with a further six apprentices joining us.

More immediate measures were necessary during 2005 to address the skills and knowledge gap that was presented by a significant reduction in specialist skills effected by the previous owner and to ensure the business was equipped with sufficient corporate skills as we made the transition to a listed company. Areas of particular focus for this recruitment activity were finance, trading and engineering.

INTERNAL COMMUNICATIONS

We use a wide variety of communication methods in order to keep people as informed as possible and eradicate confusion, conflict and misinterpretation of messages. For example, team briefings are held once a month where wide-ranging information is communicated throughout the organisation, in addition, plant-wide meetings are held on a regular basis. We have also introduced an IT-based internal feedback system, Drax Talk, allowing employees to anonymously raise concerns or make comments on any work-related issue and receive a publicly accessible response from the leadership team.

UNION REPRESENTATION

The terms and conditions of employment for the majority of staff within the Group, that is, those not employed under a personal contract, are incorporated into the Collective Agreement. This is a joint agreement between the Group and the trades unions. Staff are represented by either AMICUS, TGWU, GMB, Prospect or Unison trades unions. A positive relationship between management and trades unions has been established over a number of years and is based on clear guidelines, a consultative approach and good communication of the relevant business objectives of the Group.

Board of Directors

01 Gordon Horsfield (59)

Chairman

Appointed to the Board in October 2005, having first joined Drax in July 2003. He retired from PricewaterhouseCoopers in January 2003 after 34 years with the firm. Much of his professional career was spent as a corporate recovery specialist rising to become head of corporate finance and recovery at Price Waterhouse UK (as it was before its merger with Coopers and Lybrand in 1998) and a member of the UK firm's executive board. Following the merger with Coopers & Lybrand he was appointed to the new management board as the first director of operations of the UK firm PricewaterhouseCoopers, responsible for the new firm's finances and for pulling together and rationalising the organisational and support functions of the UK business following the merger. Subsequently he led the team dealing with the sale of its management consulting business to IBM. Gordon is also involved in a number of community activities as chair of the Council of the University of York, and as a member of the Advisory Committee to the Abbot of Ampleforth Abbey. Gordon holds a degree in Economics from the University of Nottingham and is a Chartered Accountant.

02 Dorothy Thompson (45)

Chief Executive

Appointed to the Board in October 2005, having joined Drax in September 2005. Before joining Drax, Dorothy was head of the European business of InterGen NV, the power generation subsidiary of Shell NV and Bechtel Inc. In this role, she had responsibility for the management and operation of four gas-fired power plants, totalling some 3,160MW of capacity across the UK and the Netherlands. Prior to joining InterGen in 1998, Dorothy was initially in banking and subsequently was assistant group treasurer for Powergen PLC. Dorothy holds both a Bachelor's and a Master's Degree in Economics from the London School of Economics and Political Science, London University.

03 Gordon Boyd (46)

Finance Director

Appointed to the Board in October 2005, having first joined Drax in January 2005. Gordon previously held a number of roles within British Energy plc including director of corporate restructuring, generation finance director and group treasurer. Prior to this he worked for a number of other companies including Raychem, Mothercare and Cadbury Schweppes. Gordon graduated from Edinburgh University in 1982 with a BCom (Hons). He holds an MBA and has completed the Advanced Management Program at Harvard Business School. He also holds professional accountancy (FCMA) and treasury (MCT) qualifications.

04 Peter Emery (43)

Production Director

Appointed to the Board in October 2005, having first joined Drax in June 2004. Peter achieved a First Class BSc (Hons) degree in Mining Engineering at the University of Nottingham. After leaving university, Peter joined Esso Petroleum and held a number of analyst and managerial roles in the UK before moving to Esso's parent, Exxon in the US to co-ordinate its downstream marketing and distribution investments outside North America and Canada. He returned to Esso in 1992 as plant technical services manager at Fawley Refinery. He then undertook roles managing various operational areas at the refinery before moving to refinery maintenance manager in 1997. He was appointed operations manager at Fawley Oil Refinery in 2002, having full responsibility for the management and operation of the UK's largest refinery and a member of Exxon Mobil's European leadership team for refining.

05 Tim Barker (65)

Senior Independent Non-Executive Director

Appointed to the Board in October 2005 and was appointed as the Senior Independent Director following admission to the Official List of the UK Listing Authority on 15 December 2005. He first joined Drax in June 2004. Tim is a non-executive director of Electrocomponents plc, chairman of Robert Walters plc and a member of the Professional Oversight Board for Accountancy. From 1993 he was vice chairman of Kleinwort Benson Group plc and from 1998, until his retirement in 2000, he was vice chairman of Dresdner Kleinwort Benson. Notably, he was involved with a number of clients in the energy sector and was an adviser to the UK Government on the privatisation of the electricity sector. In the mid-1980s, he was director general of the City Panel on Takeovers and Mergers.

06 Mike Grasby (62)

Independent Non-Executive Director

Appointed to the Board in October 2005, having first joined Drax in December 2003. Mike is a Chartered Engineer, FIEE and FIMechE. He retired from International Power in February 2002 after 36 years in the power industry. During his career he held a number of senior positions in the UK and international power industry with the CEEGB and National Power. He was manager of Drax Power Station between 1991 and 1995, and director of operations for National Power's portfolio, with responsibilities for over 16,000MW of generating capacity, until 1998. He was also a director of power companies in Portugal, Turkey and Pakistan. Following the demerger of National Power, he joined International Power as senior vice-president, continuing with his international directorships and leading a major consortium in the Czech Republic. He is an adviser to Manx Electricity Authority, a member of the British Energy Association (and the World Energy Council) and a director of an executive recruitment business.

07 Charles Berry (53)

Independent Non-Executive Director

Appointed to the Board following admission to the Official List of the UK Listing Authority on 15 December 2005. Charles has extensive experience within the UK power sector. He joined ScottishPower in 1991 and was appointed to the board in 1999. From 2000 to 2005, Charles was chief executive of the company's UK Operations, with responsibility for over 6,200MW of generating capacity as well as the trading business, energy retailing and strategic transactions, such as renewables development. Charles is currently a non-executive director and chairman of Eaga Group and a non-executive director of Securities Trust of Scotland plc and a former non-executive director and chairman of THUS Group plc. He holds a BSc (First Class Hons) in Electrical Engineering from the University of Glasgow and a Masters Degree in Management from the Massachusetts Institute of Technology.

08 Jamie Dundas (55)

Independent Non-Executive Director

Appointed to the Board following admission to the Official List of the UK Listing Authority on 15 December 2005. Jamie's career has been in merchant banking, finance and the property sector. Jamie spent 19 years with Morgan Grenfell Group, including ten years as a director of Morgan Grenfell & Co Limited. He was finance director of the Airport Authority, Hong Kong between 1992-96 before joining MEPC plc in 1997, initially as finance director and from 1999-2003 as chief executive. Jamie is currently a non-executive director of Standard Chartered PLC and of J Sainsbury plc and chairman of Macmillan Cancer Relief.

Directors' Report

The directors present their first report and accounts for Drax Group plc, together with the consolidated accounts of the Drax group of companies, for the year ended 31 December 2005. The directors' corporate governance and remuneration reports are set out on pages 27 to 41.

Incorporation and Admission to the Official List

Drax Group plc was incorporated on 13 September 2005 and became the holding company for the Drax group of companies on 15 December 2005 upon two schemes of arrangement (the "Schemes") taking effect. On the same day the issued share capital of Drax Group plc was admitted to the Official List of the UK Listing Authority and the Company's shares began trading on the London Stock Exchange.

Review of Operations, Current Position and Future Prospects

Details of the Group's operations for the year ended 31 December 2005, its current position and future prospects are contained in the Chairman's Statement, Chief Executive's Statement, and the Operating and Financial Review set out on pages 8 to 19.

Principal Activities

Drax Group plc is the holding company of the Drax group of companies. The principal activities of the Group are the generation and sale of electricity at the Drax Power Station, Selby, North Yorkshire and the sale of by-products of the electricity generation process. No acquisitions or disposals have been made by the Group during the year.

Going Concern

After making enquiries, the directors have a reasonable expectation that the Company and the Group as a whole will continue in operation for the foreseeable future. The directors are therefore content to adopt the going concern basis in preparing the accounts.

Results

The Group results for the year are shown in the Consolidated Income Statements on page 43.

Dividend

The directors do not recommend a final dividend for the year ended 31 December 2005.

Share Capital

During the year 406,927,661 ordinary shares each of 10 pence and 499,980 redeemable shares each of 10 pence in the Company were issued as follows:

- (1) Two ordinary shares each of £1 were issued on formation of the Company.
- (2) On 20 October 2005, the two ordinary shares each of £1 were sub-divided into 20 ordinary shares each of 10 pence.
- (3) On 20 October 2005, 499,980 redeemable shares of 10 pence each were issued to Drax Group Limited.
- (4) On 15 December 2005, upon the Schemes taking effect, 406,927,641 ordinary shares each of 10 pence were issued and the 20 ordinary shares each of 10 pence were transferred in accordance with the Schemes.

Details of the share capital as at 31 December 2005, and shares issued during the year, are given in note 5 on page 78.

Authority to Purchase Own Shares

At an Extraordinary General Meeting of the Company held on 20 October 2005, shareholders resolved to authorise the Company to make market purchases of up to 10% of the issued ordinary share capital. The authority was not used during the financial year ended on 31 December 2005. At the forthcoming Annual General Meeting, shareholders will be asked to renew this authority. Details are contained in the Notice of Meeting. The Company held no Treasury shares during the year.

Directors

The names of the present members of the Board and their biographical notes appear on page 24. The names of others who served as directors at any time in the period following incorporation and before the end of 31 December 2005 are detailed below.

	Date of appointment	Date of resignation
Luciene James Limited	13 Sep 2005	13 Sep 2005
The Company Registration Agents Limited	13 Sep 2005	13 Sep 2005
Norton Rose Limited	13 Sep 2005	20 Oct 2005
NoRose Company Secretarial Services Limited	13 Sep 2005	20 Oct 2005
Timothy Gwynne Barker	20 Oct 2005	–
Charles Andrew Berry	15 Dec 2005	–
Gordon Alexander Boyd	20 Oct 2005	–
James Frederick Trevor Dundas	15 Dec 2005	–
Peter Richard Emery	20 Oct 2005	–
Patrick Michael Grasby	20 Oct 2005	–
Gordon Christopher Horsfield	20 Oct 2005	–
Dorothy Carrington Thompson	20 Oct 2005	–

The Company's articles of association require that, following appointment by the Board, directors submit themselves for election by shareholders at the next Annual General Meeting. Each of the present directors was appointed to the Board of the Company on or after 20 October 2005 and therefore retires and offers himself or herself for re-election at the Annual General Meeting.

The articles also provide that one-third of directors shall retire by rotation each year but are eligible to submit themselves for re-election by shareholders and that directors shall not serve longer than the third Annual General Meeting following their election without being re-elected by shareholders. However, in view of the dates upon which all directors were first appointed, this provision of the articles has no practical effect in relation to the forthcoming Annual General Meeting, but it will be applied in future years.

Directors' Interests

Other than a deed of indemnity between each director and the Company in respect of claims made and personal liability incurred as a result of the bona fide discharge of their responsibilities and service contracts between the executive directors and a Group company, or as noted in the Remuneration Report, no director had a material interest at any time during the year in any contract of significance with the Company or any of its subsidiary undertakings.

Directors' Report continued

Details of directors' remuneration, service contracts and interests in the shares of the Company are set out in the Remuneration Report on pages 34 to 41.

Substantial Shareholdings

As at 7 March 2006, the Company's register of substantial shareholdings maintained in accordance with the provisions of Section 211 of the Companies Act 1985 showed that the following shareholders exceeded the 3% disclosure threshold.

	Number of ordinary shares held	% of the issued ordinary share capital held
The Capital Group Companies Inc	21,872,165	5.37
Brian J Stark	19,995,202	4.91
Legal & General Group plc	16,508,427	4.05
Deutsche Bank AG	15,048,149	3.70
Zurich Financial Services	12,306,512	3.02

Employees

Drax uses a wide variety of communication methods in order to keep employees as informed as possible. For example, team briefings are held once a month where wide-ranging information is communicated throughout the organisation. In addition, plant-wide meetings are held on a regular basis and cover, inter alia, the financial and economic factors affecting the performance of the Company.

Details of employee involvement through share participation are contained in the Remuneration Report on pages 34 to 41.

It is the Group's policy to give full consideration to suitable applications for employment from people with disabilities. In the event of a member of staff becoming disabled every effort is made to ensure that their employment with the Group continues and that appropriate training and rehabilitation is provided. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.

The Group is committed to a policy of equal opportunities and ensures that country of origin, colour, gender, religious belief, sexual orientation or disability, are not barriers to working at Drax.

Corporate Social Responsibility

Details of the Group's Corporate Social Responsibility ("CSR") policy and operations are set out on pages 20 to 23.

Charitable Donations

Drax Group has continued to support community initiatives and charitable causes and the total Group commitment during the year was £37,500 (2004: £22,750). Details of the charitable donations made are contained within the CSR report.

Political Donations

No political donations were made in the UK or elsewhere during the year (2004: £nil). It is the Board's policy not to make donations to political organisations or for political causes.

In the CSR report there is an explanation of the nature and extent of the Group's intended activities aimed only at the promotion of its business interests. The definitions attributed to EU political expenditure are broad and there is widespread doubt of the extent to which normal business activities, which might not be thought to be political expenditure in the usual sense, could be caught. In view of this the Board wishes to avoid any inadvertent infringement of the legislation by incurring unauthorised EU political expenditure and as such, is seeking the authority to incur annual expenditure, for each of the Company and its subsidiary Drax Power Limited, for such purposes of £100,000 for a period of four years. The Board does not believe that the Group has incurred any such political expenditure in the past year.

Creditor Payment Policy and Practice

Terms of payment are agreed with suppliers when negotiating each transaction and the policy is to abide by those terms and pay creditors when sums owing fall due for payment, provided that the suppliers also comply with all relevant terms and conditions. Drax Group plc, the holding company of the Group, has no trade creditors. In respect of Group activities, the amounts due to trade creditors at 31 December 2005 represented approximately 32 days of average daily purchases through the year (2004: 32 days).

Auditors

In accordance with Section 385 of the Companies Act 1985, a resolution is to be proposed at the Annual General Meeting for the reappointment of Deloitte & Touche LLP as auditors of the Company. A resolution will also be proposed authorising the directors to determine the auditors' remuneration. The Audit Committee reviews the appointment of the auditors, the auditors' effectiveness and relationship with the Group, including the level of audit and non-audit fees paid to the auditor. Further details on the work of the auditors and the Audit Committee are set out in the Audit Committee Report on pages 31 and 32.

Annual General Meeting

The first Annual General Meeting of the Company will be held on 12 May 2006 at The City Presentation Centre, 4 Chiswell Street, London EC1Y 4UP at 11am. A separate document accompanying the Directors' Report and Annual Accounts contains the notice convening the Annual General Meeting and a description of the business to be conducted.

By order of the Board



Peter Rothwell
Company Secretary
7 March 2006

Corporate Governance

Application of the Combined Code

The Listing Rules require listed companies to disclose, in relation to Section 1 of the Combined Code on Corporate Governance (the "Code"), how they have applied its principles and whether they have complied with its provisions throughout the Group's financial year. No member of the Group was obliged to comply with the Code until 15 December 2005 when Drax Group plc (the "Company") was admitted to the Official List of the UK Listing Authority and its shares began trading on the London Stock Exchange ("Listing"). This report explains the arrangements made to ensure compliance with the Code with effect from Listing but also includes references to circumstances prior to 15 December 2005. Those are references to arrangements made by the Board of Drax Group Limited, a company incorporated in the Cayman Islands and the holding company for the group until that date.

Compliance with the Combined Code

As stated above, the requirements of the Combined Code first applied to the Group on 15 December 2005. Prior to that date and from 1 January 2005, the board of Drax Group Limited applied such of the principles of the Code as it was permitted to do by virtue of the terms of the shareholders' agreement binding upon it and as the board considered both appropriate and reasonably practicable, given the financial structure and other circumstances of the group during that period. As part of its preparations for admission to the Official List of the UK Listing Authority, the Board adopted arrangements which it believes will enable it to comply throughout 2006 with substantially all of the requirements of the Code.

It is the Board's view that, throughout the period starting with Listing on 15 December and ending with the date of this report, there has been full compliance with the provisions of Section 1 of the Combined Code, with the exception that:

- (1) In the 16 day period from Listing on 15 December 2005 to the end of the year, it was not practicable for the Chairman to hold meetings with the non-executive directors as required by code provision A.1.3. However, prior to Listing, the Chairman met the non-executive directors in the absence of the executive directors on a number of occasions in relation to specific items of Board business.
- (2) As the former holder of executive office, upon appointment as Chairman, Gordon Horsfield was not independent within the meaning of code provision A.2.2.
- (3) The Board has not undertaken an evaluation of its own and of its Committees' performance as required by code provision A.6.
- (4) Whilst the Board has not conducted a review of the effectiveness of the Group's systems of internal control as required by code provision C.2.1, as part of the Listing process, the Board and its advisers formally considered those systems and their adequacy for the purposes of fulfilling the Company's obligations under the reporting requirements of the UK Listing Authority.

The Board of Directors

As at 7 March 2006 the Board comprises the non-executive Chairman, four independent non-executive directors and three executive directors.

The directors are named and their principal commitments outside the Group are described on page 24.

Gordon Horsfield is the Chairman. Between 19 April 2005 and 26 September 2005, he also undertook the role of acting Chief Executive. On 7 March 2006, upon the completion of a hand-over period following the arrival of Dorothy Thompson, he relinquished his executive responsibilities and now serves as non-executive Chairman. Gordon has held an executive position within the Company and is therefore not deemed independent within the meaning of the Combined Code. However, the Board considers it appropriate that Gordon Horsfield continues as Chairman in view of his experience and knowledge of the Company, the industry and commerce generally. The Board also considers that the short period during which he acted as Chief Executive has not adversely affected his independence of judgement.

Dorothy Thompson is the Chief Executive and is responsible for all aspects of the management of the Group and its business, including developing an appropriate business strategy for Board approval and securing its timely and effective implementation. She provides leadership to the executive team and takes responsibility for the important external relationships with customers, suppliers, regulatory agencies and government bodies. She and the Chairman maintain high quality relationships with Drax shareholders. The division of responsibilities between the Chairman and the Chief Executive is set out in writing and was agreed by the Board on 14 December 2005.

Gordon Boyd joined the Group as the Finance Director on 10 January 2005 and is responsible for the financial management of the Group, its risk management systems and systems of internal control, and for relationships with the Group's bankers.

Peter Emery is the Production Director and responsible for the operation, repair and maintenance of the electricity generation plant at Selby, North Yorkshire.

Tim Barker and Mike Grasby have served the Group as independent non-executive directors throughout the year ended 31 December 2005. The Board reviewed their position prior to the Listing and reiterated its previous conclusion that each of them is independent within the meaning of the Combined Code. On 30 November 2005, in anticipation of Listing, the Board appointed Tim Barker as senior independent director. Charles Berry and Jamie Dundas joined the Board as independent non-executive directors on 15 December 2005.

The Company's articles of association require that, following appointment by the Board, directors submit themselves for election by shareholders at the next Annual General Meeting. Each of the present directors was appointed to the Board of the Company on or after 20 October 2005 and therefore retires and offers himself or herself for re-election at the Annual General Meeting.

The articles also provide that one-third of directors shall retire by rotation each year but are eligible to submit themselves for re-election by shareholders and that directors shall not serve longer than the third Annual General Meeting following their election without being re-elected by shareholders. However, in view of the date upon which all directors were first appointed, this provision of the articles has no practical effect in relation to the forthcoming Annual General Meeting, but it will be applied in future years.

Corporate Governance continued

Each of the non-executive directors, with the exception of the Chairman, currently holds a letter of appointment which provides for the appointment to continue indefinitely subject to one month's notice of termination. The Chairman's letter of appointment provides for a fixed three year term. It is the Board's policy that each non-executive director will serve for a fixed term not exceeding 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 Annual General Meeting, may be renewed by mutual agreement. However, in the case of the independent non-executive directors, it is the Board's policy not to extend the aggregate period of service (including service as a non-executive director of Drax Group Limited) of any independent non-executive director beyond nine years and, as required by the Combined Code, subject to rigorous review any proposal to extend a non-executive director's aggregate period of office beyond six years. The Board expects to develop a programme of rotational retirement of non-executive directors as a result of which the skills and experience available to the Board will be refreshed periodically.

The Board has adopted a schedule of matters reserved for its decision and formal terms of reference for its committees which are available on the Group's website (www.draxgroup.plc.uk). The Board determines: the Group's strategy; 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 Board structure, composition and succession. 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 Chief Executive or otherwise delegated in accordance with a scheme of delegation approved by the Board.

The Board receives regular reports on performance against the Business Plan and periodic business reports from senior management. Via a committee, the Board monitors risk exposures against risk management policies. Directors are briefed on matters to be discussed at meetings by papers distributed in advance of Board and committee meetings.

The Board is satisfied that all the directors are able to devote sufficient time to their duties as directors.

The Board has adopted a policy whereby directors may, in the furtherance of their duties, seek independent professional advice at the Company's expense. No director obtained any such advice during 2005.

During the year ended 31 December 2005, each of the appointments of Charles Berry, Jamie Dundas, Dorothy Thompson and Gordon Boyd was made on merit and after a selection process, conducted with the aid of recruitment consultants, which assessed candidates against objective criteria determined in advance.

As mentioned in the Directors' Report, each director has the benefit of a deed of indemnity from the Company and its subsidiaries in respect of claims made and liabilities incurred, in either case arising out of the bona fide discharge by the director of his or her duties. The Company has also arranged appropriate insurance cover in respect of legal action against its directors.

Committees of the Board

The Board, and where indicated below, its predecessor, the board of Drax Group Limited has (or had) established the following standing committees:

- (1) Audit Committee which, following Listing, comprises Tim Barker (as Chairman), Charles Berry and Jamie Dundas. It is the current intention that Jamie Dundas will take over as Chairman of the Committee immediately after the Annual General Meeting on 12 May 2006. Prior to Listing (and as a committee of the board of Drax Group Limited), the committee comprised Tim Barker (as Chairman), Gordon Horsfield and Mike Grasby.
- (2) Remuneration Committee which, following Listing, comprises Tim Barker (as Chairman), Charles Berry, Jamie Dundas and Mike Grasby. Prior to Listing (and as a committee of the board of Drax Group Limited), the committee comprised Gordon Horsfield (Chairman), Tim Barker and Mike Grasby.
- (3) Nominations Committee which was established on Listing comprises Gordon Horsfield (as Chairman), Tim Barker, Charles Berry, Jamie Dundas and Mike Grasby.
- (4) Health and Safety Committee comprises Mike Grasby (as Chairman), Dorothy Thompson and Peter Emery, with the Safety Manager in attendance. Prior to Listing, the board of Drax Power Limited had established a Company Health and Safety Committee.

The Board also has a Trading and Risk Management Committee whose core function is to monitor the effectiveness of risk management in relation to trading and treasury matters. It comprises Gordon Boyd (as Chairman), Gordon Horsfield, Dorothy Thompson and Peter Emery. Prior to Listing, the board of Drax Power Limited had established a Risk Management Committee which, throughout 2005 until Listing, undertook a role similar to that of the Trading and Risk Management Committee of the Board. The Board is minded to review the role and membership of this committee.

Details of the work of the Audit, Nominations and Remuneration Committees are given in the reports of those Committees on pages 31 to 41.

Board and Board Committee Attendance 2005

From Listing (the date upon which the Combined Code first applied) and until 31 December 2005, the Board of Drax Group plc and its Remuneration Committee each held one meeting. There were no meetings of the Audit or Nominations Committees in that period.

During the period commencing 1 January 2005 and ending 14 December 2005, the Board of Drax Group Limited and its Audit and Remuneration Committees held a number of meetings. The number of meetings of the board of Drax Group Limited was unusually high owing to the demands, first of the Refinancing and Listing completed on 15 December 2005 and secondly of the three proposals to acquire the Group received after 1 September 2005 and prior to Listing.

The number of meetings of the Remuneration Committee of Drax Group Limited was unusually high because of the business (a) occasioned by the Prospectus and the Listing, (b) arising out of the vesting of shares from the Drax Group Limited Long-Term Incentive Plan, and (c) the development of share schemes for implementation after Listing.

The table below shows the number of meetings and attendance at them by directors of each the Board and Remuneration Committee of Drax Group plc and of the Board, Audit and Remuneration Committees of Drax Group Limited.

The number in brackets represents the maximum number of meetings that each individual was entitled to and had the opportunity to attend.

	Drax Group plc		Drax Group Limited		
	Board	Remuneration Committee	Board	Audit Committee	Remuneration Committee
Tim Barker	1 (1)	1 (1)	16 (17)	6 (6)	8 (8)
Charles Berry	1 (1)	1 (1)	0 (0)	0 (0)	0 (0)
Gordon Boyd	1 (1)	0 (0)	17 (17)	0 (0)	0 (0)
Jamie Dundas	1 (1)	0 (1)	0 (0)	0 (0)	0 (0)
Peter Emery	1 (1)	0 (0)	17 (17)	0 (0)	0 (0)
Mike Grasby	1 (1)	1 (1)	15 (17)	5 (6)	8 (8)
Gordon Horsfield	1 (1)	1 (1)	16 (17)	6 (6)	8 (8)
Dorothy Thompson	1 (1)	0 (0)	6 (6)	0 (0)	0 (0)
Gerald Wingrove*	0 (0)	0 (0)	3 (4)	0 (0)	0 (0)

* Resigned directorships of all group companies on 19 April 2005.

Performance Reviews and Directors' Development

The board of Drax Group Limited did not undertake an evaluation of its performance or of that of its committees during 2005, nor has the Board of the Company done so in the period from 15 December 2005 to the end of the financial year on 31 December 2005. However, it is the intention of the Board to undertake formal reviews of its own performance, of its Committees and of individual directors towards the end of 2006.

As stated in its report on pages 34 to 41, in January 2006, after the end of the year, the Remuneration Committee evaluated the performance of executive directors. That review was informed by the opinions of Tim Barker and Mike Grasby who met in the absence of executive directors to evaluate the performance of the Chairman. Both evaluations were informed by the results of a confidential survey of senior managers' opinions. As explained earlier, in the 16 day period between Listing on 15 December and the end of the year it was not practicable for the Chairman to hold meetings with the non-executive directors in the absence of the executive directors as required by code provision A.1.3 of the Combined Code. However, earlier in the year, as Chairman of Drax Group Limited, the Chairman met with the non-executive directors in the absence of the executives on a number of occasions in relation to specific matters of concern to the Board.

The Board is committed to the development of all employees and directors and intends to review individual director's development requirements and make appropriate arrangements to address them. Induction programmes have been arranged for Charles Berry and Jamie Dundas.

Relations with Shareholders

The Company places considerable importance on communication with shareholders and engages with them on a wide range of issues. During 2005 a Head of Corporate Affairs joined the Group. During the coming year he will assist in developing appropriate liaison and dialogue between the Group and its major shareholders. In the months prior to Listing, the Chairman and the other executive directors met on a number of occasions with the shareholders of Drax Group Limited and also with a large number of prospective shareholders of the Company.

Corporate Governance continued

The Company's small and private shareholders together hold approximately 1.85% of the issued share capital. The Board is as interested in their concerns as in the concerns of larger shareholders. All shareholders are free to put questions to the Board at the Annual General Meeting. Questions asked in person at the Annual General Meeting will receive an oral response whenever possible. Otherwise a written response will be provided as soon as practicable after the meeting. Questions asked at other times will normally receive a written response. Shareholders attending the Annual General Meeting 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 appears on the Group's website within a matter of hours.

This Annual Report and Accounts together with other public announcements is designed to present a balanced and understandable view of the Group's activities and prospects. The Chairman's Statement, Chief Executive's Statement, and Operating and Financial Review on pages 8 to 19 provide an assessment of the Group's affairs. This Annual Report is being despatched to shareholders at least 20 working days before the Annual General Meeting and the accompanying Form of Proxy provides for a shareholder to indicate abstention as an alternative to a vote in favour or against each separate resolution. Particulars of aggregate proxies lodged will be placed on the Group's website as soon as practicable.

Directors' Responsibilities

The directors are responsible for preparing the Annual Report and the financial statements. The directors are required to prepare financial statements for the Group in accordance with International Financial Reporting Standards (IFRS). Company law requires the directors to prepare such financial statements in accordance with International Financial Reporting Standards, the Companies Act 1985 and Article 4 of the IAS Regulation.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Group's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's "Framework for Preparation and Presentation of Financial Statements". In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards. Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- provide additional disclosures when compliance with specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

The directors are responsible for maintaining proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a directors' report and directors' remuneration report which comply with the requirements of the Companies Act 1985.

The directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

The Independent Auditors' Report on page 42 summarises their review of the Company's compliance with the relevant provisions of the Combined Code as applicable to the Company during the year under review.

Audit Committee Report

The Audit Committee of the Board (the "Committee") was established on Listing on 15 December 2005 and did not meet during the year ended 31 December 2005. It has, however, met since 31 December 2005 for the purpose of considering the outcome of the audit of the accounts for the year ended 31 December 2005 and the draft of this Annual Report and to make appropriate recommendations to the Board.

This report, therefore, describes the role of the Committee and of the work undertaken by the Audit Committee of the board of Drax Group Limited (the "Former Committee") which was the holding company of the Drax Group until Listing. The purpose of the Committee is (and of the Former Committee was) to assist the Board in discharging its responsibilities for the integrity of the Company's financial announcements, the assessment of the effectiveness of the systems of risk management, internal control and regulatory compliance and to oversee the objectivity and effectiveness of the internal audit function (which is undertaken, under the direction of the Finance Director, by an independent leading firm of accountants) and of the external auditors. A copy of the Committee's terms of reference is available on the Company's website (www.draxgroup.plc.uk).

The Audit Committee

The Committee currently comprises the following independent non-executive directors, appointed by the Board:

Tim Barker (Chairman of the Committee)
Jamie Dundas
Charles Berry

Prior to Listing, the Former Committee comprised: Tim Barker (as Chairman); Gordon Horsfield (Chairman of the Board); and Mike Grasby. Tim Barker and Mike Grasby were independent non-executive directors.

It is the current intention that Jamie Dundas will take over as Chairman of the Committee immediately following the Annual General Meeting on 12 May 2006.

The Former Committee met on six occasions in 2005 and the members' attendance record is set out on page 29. The Company Secretary acted as the Secretary to the Former Committee and acts as Secretary to the Committee.

The biographies of the directors who are members of the Committee are set out on page 24. The Board is satisfied that all these directors have recent and relevant financial experience.

The Chief Executive, the Finance Director and the external auditors normally attended, by invitation, all meetings of the Former Committee and it is intended that they shall normally attend all meetings of the Committee. Other members of senior management were also present at meetings of the Former Committee (and will be invited to attend meetings of the

Committee) as appropriate in order to present reports. In undertaking its duties, the Former Committee had, and the Committee has, access to the services of the Finance Director and the Company Secretary and their resources, as well as access to external professional advice.

The Committee intends to undertake its duties in line with an agreed annual work plan. It will review, with members of management and the external auditors, the Company's formal financial announcements. It reviewed this Annual Report and Accounts to shareholders and associated documentation before publication, with a particular emphasis on their fair representation and the reasonableness of the judgemental factors and appropriateness of significant accounting policies used in their preparation. On a regular basis, it will receive reports on risk management, fraud, legal and corporate governance matters, in order to help it assess the effectiveness of the risk management and control frameworks. The Committee will also periodically review the Company's arrangements in respect of its "whistleblowing" policy in order to ensure that the arrangements allow proportionate and independent investigation of matters raised and that appropriate follow up actions are in place.

With the implementation of International Financial Reporting Standards (IFRS) for the 2005 financial year and in respect of the Prospectus published prior to Listing, the Former Committee reviewed the progress of the Group's preparations for reporting under the new standards and the related processes that have been embedded throughout the Group.

The Committee will receive reports from the external auditors and will hold discussions with representatives from the audit firm, in the absence of management. In order that the Board is kept fully apprised of the Committee's work, the Chairman of the Committee will follow the practice of the Chairman of the Former Committee and report the Committee's deliberations to the next following Board meeting. The Board will receive a copy of the minutes of each meeting of the Committee.

Internal Controls

The Board has the ultimate responsibility for the systems of internal control maintained by the Group and for reviewing their effectiveness. The systems are intended to provide reasonable assurance, but not an absolute guarantee, against material financial misstatement or loss, and include the safeguarding of assets, the maintenance of proper accounting records, the reliability of financial information, compliance with appropriate legislation, regulation and best practice, and the identification and containment of business risks.

The Committee, acting on behalf of the Board, will undertake an annual review of the effectiveness of, and the framework for, the Group's systems of internal control. In the Board's view, the information it will receive will be sufficient to enable it to review the effectiveness of the Group's systems of internal control in accordance with the Guidance on Internal Control issued for the purposes of the Combined Code.

Audit Committee Report continued

The principal features of the control framework are as follows:

Control Environment

The Group has an established governance framework. The key features of the control environment within the framework include: the Statement of Matters Reserved to the Board and the terms of reference for each of its committees; a clear organisational structure, with documented delegation of authority from the Board to executive management; a Group policy framework, which sets out risk management and control standards for the Group's operations; and defined procedures for the approval of major transactions, budgets and capital allocations. Further details on financial and capital risk management are given in the Operating and Financial Review on pages 12 to 19.

Risk Identification, Assessment and Management

The Group has an established system of business risk management, which is integrated into the Group's business planning and performance monitoring processes. The Group's risk management and control framework is designed to support the identification, assessment, monitoring and control of risks that are significant to the achievement of the Group's business objectives. Policies and controls pertinent to the Group's trading operations and actual performance in relation to them are kept under review by the Trading and Risk Management Committee.

Control Procedures and Monitoring Systems

The Group has a system of planning and monitoring, which incorporates Board approval of a rolling five-year Business Plan and approval towards the end of a year of operating and capital expenditure budgets for the year ahead. Performance against the budget is subsequently monitored and reported to the Board each time it meets. The Board also receives regular reports from the Trading and Risk Management Committee. Performance is also reported formally through the publication of Group results, and accounting policies are applied consistently throughout the Group. Operational management report frequently to the executive directors.

Internal Audit

Under the direction of the Finance Director, the Group has outsourced the internal audit function to Grant Thornton UK LLP, which is an independent leading firm of accountants. They undertake the full range of reviews that would ordinarily be undertaken by an internal audit function. Regular reports are provided to the Committee regarding the audit programme and audits undertaken and recommendations are made to management for process improvements as appropriate.

External Auditors

Deloitte & Touche LLP were appointed as auditors of the Company in 2005, having previously acted as auditors to the group companies of which Drax Group Limited was then the holding company. The audit engagement partner changed as part of a rotation process in 2003. Deloitte & Touche LLP audits all companies in the Group which are not dormant.

The Company has a formal policy aimed at safeguarding and supporting the independence of the auditors by avoiding conflict of interests. The Former Committee reviewed compliance with the policy concerning the use of the external auditor in non-audit work. The Committee intends to apply the best practice recommendations in the Combined Code and intends to adopt and pursue a policy which regulates the appointment of former audit employees into senior finance positions within the Group and sets out the approach to be taken by the Group when using the services of the auditor, distinguishing between those matters where the Company requires an independent view, such as audit and assurance work, from other advisory services. In addition to statutory audits, audit and assurance work includes reviewing statutory returns, due diligence associated with acquisitions and disposals, fraud investigations and control and audit reviews. Whilst the aim is to ensure that the auditor cannot be engaged for any other purpose, it is recognised that there may be a small number of areas where, for pragmatic reasons, it may be in the Group's interests to use the external auditor for other work.

Audit Committee Report

The Committee will review annually a formal letter provided by the external auditors confirming its independence and objectivity within the context of applicable regulatory requirements and professional standards and did so in the period leading up to its approval of this Annual Report and Accounts.

This report was reviewed and approved by the Board on 7 March 2006.



Tim Barker
Chairman
Audit Committee

Nominations Committee Report

The Nominations Committee of the Board (the "Committee") was first established on Listing on 15 December 2005 and did not meet before the end of the year. This report provides details of the role of the Committee and the work it will ordinarily undertake during a year.

The Committee currently comprises the following directors, appointed by the Board:

Gordon Horsfield (Chairman)
Tim Barker
Charles Berry
Jamie Dundas
Mike Grasby

The Company Secretary acts as the Secretary to the Committee. The terms of reference of the Committee require it to deal with the constitution of the Board and to consider the succession of the directors. The Committee will review the skills, experiences and independence of its directors and, as appropriate, will identify and assess potential new directors. It will also review those directors retiring by rotation in accordance with the Company's articles of association with a view to making recommendations to the Board regarding their re-election.

A copy of the Committee's terms of reference is available from the Company Secretary and can be viewed on the Company's website (www.draxgroup.plc.uk). In undertaking its duties the Committee will monitor the skill requirements of the Board and the knowledge, experience, length of service and performance of the directors. It will also review their external interests with a view to identifying any actual or perceived potential conflict of interests, including the time which they are able to commit to their duties as directors of the Company. The Committee will also monitor

matters relating to the independence of each non-executive director. The results of these reviews will be taken into account when the Board considers succession planning and the reappointment of directors. Members of the Committee will take no part in any discussions concerning their own circumstances.

Directors' service contracts 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, prior to the Annual General Meeting, details of which are contained in the Notice of Meeting.

As stated in this report, the Committee has not met, but has set out the manner in which it will conduct itself. Prior to the Listing and prior to the requirement for the Committee, the group had in place a robust and fair process by which it selected and appointed Gordon Boyd and Dorothy Thompson and, at the time of Listing, Charles Berry and Jamie Dundas. The process included, but was not limited to, the use of external recruitment advisers deemed to have the relevant experience for recruitment of personnel at this level and also the Chairman and each serving director had discussions with the proposed candidates prior to the final appointment being made.

This report was reviewed and approved by the Board on 7 March 2006.


Gordon Horsfield
Chairman
Nominations Committee

Remuneration Report

Drax Group plc (the "Company") became the holding Company for the Drax group of companies on 15 December 2005 upon its admission to the Official List of the UK Listing Authority ("Listing"). The Remuneration Committee of the Board of the Company (the "Committee") became responsible for matters relating to remuneration on that date. Until that date Drax Group Limited was the holding company of the Drax group and the Remuneration Committee of its Board (the "Former Committee") was responsible for the matters dealt with in this report. Whilst compliance with the Combined Code and with the Directors' Remuneration Report Regulations has been required only since Listing, the Remuneration Committee believes that an understanding of the work of both committees is necessary for a fair report to be given. A copy of the Committee's terms of reference is available on the Company's website (www.draxgroup.plc.uk).

Part 1: Unaudited Information

REMUNERATION COMMITTEE

The members of the Remuneration Committee appointed by the relevant Board are as follows:

	Members of the Remuneration Committee of the Board of	
	Drax Group Limited (until 15 December 2005)	The Company (on and from 15 December 2005)
Gordon Horsfield	Chairman of the Committee	-
Tim Barker ⁽¹⁾	✓	Chairman of the Committee
Mike Grasby ⁽¹⁾	✓	✓
Charles Berry ⁽¹⁾	n/a	✓
Jamie Dundas ⁽¹⁾	n/a	✓

(1) Independent non-executive director.

There were eight meetings of the Former Committee during the period ended on 31 December 2005 and one meeting of the Committee. Except for Jamie Dundas who was unable to attend the meeting on 20 December 2005, all other members of the Former Committee or the Committee respectively attended all the meetings.

The Committee recommends to the Board a remuneration framework designed to allow the Company to attract and retain its executive directors and senior management and which is aligned to shareholder interests. Within that framework, it determines the remuneration of executive directors and senior management, including pension rights and any compensation payments. In addition, it is responsible for setting the remuneration of the Chairman and maintains an overview over rewards for all other employees.

Whilst he was Chairman and a member of the Former Committee, Gordon Horsfield took no part in discussions relating to his own remuneration, bonus awards or awards under the Drax Group Long-Term Incentive Plan ("LTIP") which vested upon Listing.

The Committee has noted the change to international accounting standards in 2005 and the adoption of European Embedded Value principles. The Committee will continue to monitor the impact of these regulations on remuneration policy and performance conditions for incentive plans.

ADVISERS

The Committees have retained Peter Newhouse & Co to advise them throughout the period and that firm has not provided any other services to the Group during, or since the end of, the period.

The Committees have also had the support of John Readshaw, Head of Human Resources at Drax who has also acted as Secretary to both Committees.

CHAIRMAN AND NON-EXECUTIVE DIRECTORS' REMUNERATION

The Chairman served in an executive capacity throughout 2005. Particulars of his remuneration during the year are set out in Part 2 of this report. On 7 March 2006, upon the relinquishment by him of his executive responsibilities (as foreshadowed in the Listing Particulars), the Chairman's service agreement was terminated by mutual consent and without cost to the Group. As a non-executive he has a contract to provide services in substantially similar terms to the contract with each of the other non-executive directors, save as to the level of remuneration and the period of notice to terminate the contract. On the basis of a review of remuneration data for Chairmen of other listed PLCs of a similar market value or turnover to Drax and having regard to his expected time commitment, the Committee determined that Gordon Horsfield should be paid a fee of £185,000 per annum for his services as non-executive Chairman and that his notice period should be six months on either side. Like the other non-executive directors, he will not receive a pension or other benefits, nor will he participate in the annual cash bonus or any of the share-based reward schemes being introduced during 2006. Gordon Horsfield agreed that, in view of the stage reached in the transfer of his executive responsibilities to Dorothy Thompson, his salary as an executive director should be reduced to £185,000 per annum and he should forego his right to bonus and other benefits under his service agreement in respect of the period from 1 February 2006 to 7 March 2006.

The remuneration for the other non-executive directors is determined by the Chairman and executive directors and is designed to: i) recognise prevailing market rates for non-executive directors' fees; ii) reflect the responsibilities and time commitment of non-executive directors; and iii) attract and retain individuals with the necessary skills and experience to contribute to the future growth of the Company. The non-executive directors are paid a basic monthly fee of £3,000 with additional fees of £420 per month for each Board Committee membership. These fees are neither performance related nor pensionable. The non-executive directors do not participate in any of the Company's bonus or share schemes. The fees for non-executive directors were originally set at the end of 2003 and, whilst they have since been reviewed regularly, they have not been changed. The non-executive directors have contracts to provide services to the Company which may be terminated by either party at any time on giving one month's notice. Fees for non-executive directors will again be reviewed during 2006.

During 2005, substantial additional time beyond that contemplated in their agreements was necessarily devoted to the affairs of the Group by Tim Barker and Mike Grasby, two of the non-executive directors. Time records show that they each devoted the equivalent of 54 days to Drax against the equivalent of 18.5 days contemplated by Tim Barker's contract and 21 days by Mike Grasby's. The causes of this additional time primarily fell into three areas: first, the need to recruit three additional directors to the Board, including a new Chief Executive; secondly, the consideration and handling of three indicative bids for the Group's business during the Autumn of 2005; and thirdly the implications of the Refinancing and Listing itself. The latter included the review and consideration of numerous documents, including published documents involving the acceptance of personal responsibility for their content. After taking advice from the Company's solicitors, its

brokers and its remuneration consultant, the executive directors, the new non-executive directors and the Chairman were minded to pay additional remuneration pro-rata to the additional time commitment. This proposal was discussed with representatives of the Association of British Insurers and with a number of the Company's major shareholders representing in aggregate more than 27% of the shares in issue at 31 January 2006, before being approved by the Board (Tim Barker and Mike Grasby taking no part in the discussion). The approved additional payments to the two non-executive directors, are as follows:

- Tim Barker £88,424
- Mike Grasby £80,331

EXECUTIVES' REMUNERATION POLICY

The Committees have consistently pursued the following remuneration policy in respect of executive directors and other management staff since the Former Committee was first established early in 2004. The Committee intends to continue to apply the same policy in 2006 and thereafter. The policy is to:

- base an increasing proportion of total pay on performance;
- manage salaries and benefits around median levels using both industry and cross-industry benchmarks;
- award annual cash bonuses which are firmly linked to the delivery of Drax's annual Business Plan targets and personal performance; and
- provide all our staff with long-term incentives linked to the value of Drax's shares and its performance.

The objectives of the policy are to:

- strengthen teamwork at all levels;
- motivate executive directors and staff to ensure that Drax meets challenging performance goals; and
- enable Drax to recruit and retain the expertise needed to consolidate and develop its business.

IMPLEMENTATION OF POLICY

The remainder of this section of the report explains how this policy is applied to executive directors with a view to attracting and retaining quality individuals and motivating them to deliver sustained performance improvements. The balanced reward package includes meaningful performance-related bonus opportunities, both over the short and the longer term.

Total rewards for executive directors comprise base pay, benefits in kind, pension and variable pay (annual cash bonus and long-term incentive plans). An indication of the relative significance of each of these components for 2006 and thereafter is given later in this report.

A) BASE PAY

Base pay and benefits are reviewed annually from 1 April and are determined having regard to the levels paid in a comparator group of utilities, power generators and other industrial companies with a similar turnover or market value. The policy is to set base pay at levels at or about the median point evident from the comparator group. For 2005, the Company's executive directors were generally paid salaries below the market median for industrial companies with a similar turnover as reported in the Monks Partnership Management Pay Report. The Former Committee consulted that publication annually when reviewing the salaries of executive directors and the Committee intends to continue that practice. Directors' base pay during 2005 is shown in the emoluments table in Part 2 of this report.

The following table sets out the current annual packages for the directors. Except for Gordon Horsfield (see note 5 below), the figures are those effective as of 1 January 2006 and assume "on-target" performance for bonus purposes. The table excludes benefits under the Executive Share Incentive Plan ("ESIP") (see below) pursuant to which no awards have yet been made. The Committee intends to review the annual salaries of the executive directors with effect from 1 April 2006.

	Annual salary £'000	Annual fee ⁽¹⁾ £'000	Annual cash bonus ⁽²⁾ £'000	Annual benefits ⁽³⁾ £'000	Annual pension ⁽⁴⁾ £'000	Total "On Target" £'000
Gordon Horsfield ⁽⁵⁾	–	185	–	–	–	185
Mike Grasby	–	51	–	–	–	51
Tim Barker	–	51	–	–	–	51
Jamie Dundas	–	51	–	–	–	51
Charles Berry	–	51	–	–	–	51
Dorothy Thompson	350	–	140	18	70	578
Peter Emery	175	–	70	12	35	292
Gordon Boyd	190	–	76	12	38	316

(1) Includes Board Committee membership fees paid as separate amounts.

(2) Annual Cash Bonus assumes an "on target" performance yielding a bonus of 40% of base salary.

(3) Represents directors' car allowance only – other benefits such as BUPA and additional life cover are variable according to personal circumstances.

(4) Annual contribution by the Company to the directors' pension plan or cash in lieu.

(5) The figure shown is Gordon Horsfield's annual fee as a non-executive director with effect from 7 March 2006. During January 2006 his salary as an executive director was £295,000 per annum. With effect from 1 February, by mutual agreement, his salary was reduced to £185,000 per annum and he agreed to forego bonus, pension, car allowance and other benefits from that date.

B) BENEFITS IN KIND

Our policy is to offer a car allowance to executive directors and, according to their role, to senior managers. This ranges currently from £17,500 per annum for the Chief Executive and £12,000 per annum for executive directors to £4,800 for certain senior managers. In addition, private medical insurance for the director and dependants, and life insurance (in a sum assured of four times basic salary) are provided. Relocation expenses are paid where appropriate. Executive directors receive no other benefits in kind.

Remuneration Report continued

C) PENSIONS

Drax Power Limited is the principal employer of the Drax Group of the Electricity Supply Pensions Scheme which is an occupational pension scheme providing defined benefits on the member's death, ill-health, early retirement or retirement to eligible members and beneficiaries based on members' length of pensionable service, final salary and the applicable accrual rate. The defined benefit Pension Scheme was closed to new entrants in 2002. Although certain senior managers are members, none of the executive directors are eligible for membership.

Executive directors and those senior managers who joined the group after 1 January 2002 are entitled to membership of the Group's defined contribution pension plan. The employer's contribution for senior managers is 11.5% of basic pay (up to currently permitted maximum pay for tax deductible contributions of £105,600 per annum for 2005). The employer's contribution in respect of executive directors who join the plan is 20% of basic pay up to the currently permitted maximum pay for tax deductible contributions, with any balance of entitlement being paid as cash and subject to normal statutory deductions. Alternatively, at their option, executive directors may either have contributions of the same amounts made to their personal pension schemes or they may choose to be paid cash in lieu of pension at the stated rate and subject to normal statutory deductions. Details of the pension contributions for executive directors and of payments in lieu are included in the emoluments table in Part 2 of this report.

D) VARIABLE PAY

Variable pay has formed a significant proportion of the potential total pay of executive directors since the end of 2003 and it is the Committee's intention to ensure that a significant proportion of total potential pay continues to be at risk of performance.

During 2005, the two components of variable pay for executive directors and senior managers were an annual cash bonus and participation in the LTIP. For 2006 there will also be a cash bonus (with the same performance-related structure as, but different performance targets to, the 2005 bonus and with increased emphasis upon personal performance). However, participation in the LTIP (which matured on Listing) will be replaced by participation in the new ESIP, details of which are given on page 37.

ANNUAL CASH BONUS

During 2005, executive directors were able to earn a bonus of up to 60% of base pay (with an on target bonus of 40% of base pay). Senior managers were able to earn up to 50% of base pay (with an on target of 33%) by way of bonus.

Performance targets for the 2005 annual bonus were set by the Former Committee at the end of 2004 and were designed to incentivise executive directors to deliver and exceed the targets set by Drax Power's Business Plan for 2005. The targets incorporated a mixture of financial, trading, plant, safety, environmental and development objectives.

When determining the annual bonus for executive directors and senior managers, the Committee has regard not only to the performance of the Company against its Business Plan targets but also the personal performance of the individual.

For 2006 the Committee will continue this approach, so as to incentivise executive directors and senior managers to deliver and exceed the Company's Business Plan.

LONG-TERM INCENTIVES

The Committee believes that employee share ownership plays a significant role in the recruitment, motivation and retention of staff at all levels within Drax.

AWARDS UNDER THE DRAX GROUP LIMITED LONG-TERM INCENTIVE PLAN (LTIP)

The LTIP was approved by resolution of the shareholders of Drax Group Limited ("DGL") passed at an Extraordinary General Meeting on 30 April 2004 (the "EGM"). It is summarised in note 21 to the Consolidated Financial Statements on pages 63 to 65 which explains that:

- (1) All employees were capable of benefiting from the LTIP which would have available to it a cash pool of £5.1m and a share pool of 4,323,600 non-voting shares in DGL (equivalent at Listing to 12,970,800 shares in the Company);
- (2) Awards were to take the form of: (a) Initial Awards of shares to be purchased before 31 May 2004 by beneficiaries at 13.65 pence per DGL share (considered by the directors to be in excess of the value of a non-voting share, having regard to the restricted rights attaching to that class of shares and the value at which the DGL debt, to which its shares were stapled, was then trading); (b) cash "points" giving a proportionate right to a share of the £5.1m pool conditionally upon the repayment of the company's debt and the beneficiary continuing to be employed by the group; and (c) share "points" giving a proportionate right to the balance of the share pool after allowing for the Initial Awards.
- (3) The conditional right to shares given by the share points would vest, provided the beneficiary was still employed by the group, upon an "Exit" event (the Listing was such an event).

Whilst the Former Committee had the discretion to award benefits as it saw fit, it was explained in the circular to shareholders for the EGM that the policy would be to allocate approximately 25% of each of the cash and share points as Initial Awards and that the balance would be allocated over the following three years, broadly on the basis of one third to directors, one third to other management and the remaining third among all other staff with more than one year's service at the time of an Exit event.

During 2005, particularly after the process leading to the Listing began in Spring 2005, the Former Committee sought to apply these principles in the context of changed circumstances which included:

- (1) the departure of the former Chief Executive and the temporary assumption of his responsibilities by the Chairman; and
- (2) the significant number of new employees who joined between December 2003 and the middle of 2005, particularly senior managers needed to meet the needs of the newly independent business.

The Former Committee concluded that the proportion of the cash and share pools available for directors should be reduced to 26% and that the value released should be distributed between the management groups (excluding directors) and all other employees. A decision was made to award points to all employees in service at Listing with awards being adjusted in most cases to reflect length of service. Except for directors and members of the management group's entitlement to the full per capita award depended on 36 months' service, with awards to those with less service being proportionately reduced. Of the total cash and share pools, some 72% of the cash and 74% of the shares were awarded otherwise than to directors.

The effect, as at Listing, of awards to directors under the LTIP is shown in a table in Part 2 of this report.

With a view to evidencing their commitment to the group at the time of Listing, the Chairman and all executive directors, together with other members of the management team, voluntarily entered into lock-in restrictions on the sale of shares in the Company which they held or received in consequence of awards made to them under the LTIP. These restrictions require that, after share sales sufficient to meet income tax and employee's national insurance liabilities arising on the Listing, the personnel concerned will continue to hold (subject to limited rights of transfer to connected parties) at least one half of the remaining shares for at least one year following the Listing. Substantially similar restrictions also apply to defer payment of half of the cash element receivable under the LTIP.

FUTURE SHARE-BASED AWARDS

As explained in the Listing Particulars, the Company has adopted three share-based plans to provide long-term incentives for its executive directors, senior managers and all other employees:

1. Executive Share Incentive Plan ("ESIP"). The Remuneration Committee currently envisages that participation will be limited to executive directors and the Group's senior managers.

Contingent awards over ordinary shares in the Company are intended to be made by the Remuneration Committee annually under the plan. Subject to continued employment, these awards, or some proportion of them, will vest over three to five years. Except to the extent determined by the Committee in the case of a beneficiary leaving the Group in defined circumstances and before the end of an ESIP cycle, no part of an award will vest less than three years after the date it was made. The value at maturity of an award will depend on the performance of the Company as determined by reference to: i) a comparison of Drax total shareholder return with those companies comprising the FTSE 250; and ii) the internal performance of the Company measured by an annual performance index, the value of which will depend on performance against the objectives contained in the Business Plan. Below a minimum performance hurdle, no shares will vest.

The Committee has under consideration whether to incentivise beneficiaries better during the five years following each of their first three awards by providing for early vesting of parts of each of those awards: that is, subject to the performance conditions, 25%, or thereabouts, of each of the first two awards would vest after three and four years and 25%, or thereabouts, of the third award would vest after four years.

It is the Committee's current intention to launch the ESIP shortly and that, subject to the Committee deciding that: i) the details of the calculation and application of the ESIP index (mentioned below) have been settled to its satisfaction; and ii) it is satisfied with the mechanism by which partial early vesting of the first three awards is to be implemented, the plan should operate in accordance with the following principles:

- An ESIP cycle with a duration of five years (subject to any early vesting provisions for the first three awards) starts every year.
- Drax employees participate in the ESIP at the invitation of the Remuneration Committee.
- At the start of each ESIP cycle, each participant will be set an Initial Award comprising a number of Drax shares. The Initial Award represents a "target" number of shares to be awarded at the end of the cycle, subject to the achievement of performance conditions.
- During the ESIP cycle, the performance of the Company will be assessed annually by the Remuneration Committee against the external and internal performance criteria referred to above and the Company's performance will be expressed as an annual ESIP Performance Index in the range 0 to 150% with 100% representing "on target" performance.
- Under the partial vesting proposals for the first three Initial Awards, the number of shares from the Initial Award vesting less than five years from the date of the award will be the Initial Award multiplied by the percentage due to vest in the year, multiplied by a Performance Factor ("PF") for the period since the date of the Initial Award. The PF will be the result of multiplying together the annual ESIP Performance Index values since the date of the Initial Award.
- The Final Award of shares at the end of the ESIP cycle will be the Initial Award (that is, the target number of shares), multiplied, in the case of awards subject to partial early vesting, by the percentage of the Initial Award which has not already vested, multiplied by a Performance Factor for the ESIP cycle which is the result of multiplying together the annual ESIP Performance Index values during the term of the award.

It is the Committee's intention that participants in the ESIP should receive an Initial Award of shares equivalent in value (as of the award date) to the annualised cash bonus they were paid in respect of 2005 or the "on target" annual bonus for new joiners.

2. A Share Incentive Plan ("SIP") approved by HM Revenue & Customs. Participation is open to all employees, including executive directors. Subject to the limits in, and other provisions of, the applicable legislation, the scheme allows the Committee to make to each participating individual free share awards worth not more than £3,000 in any tax year and, within lower financial limits, to allow the tax-free purchase of ordinary shares and the re-investment in shares of dividends on shares already purchased. Grants of free shares may reflect the degree to which performance targets have been attained and may be subject to forfeiture if the participant voluntarily leaves the employment of the Group within three years. Shares purchased must be held for a minimum period of five years for the participant to secure the full tax advantage allowed by the scheme.

It is the Committee's intention to launch the SIP shortly and annually in subsequent years and that the plan should operate as follows:

- All Drax employees will be invited to participate in the SIP (subject only to such restrictions as are imposed on participation by HM Revenue & Customs).
- All Drax employees should have an Initial Award of shares equivalent in value (as of the award date) to £2,000.
- From 2007, the actual value of shares awarded each year shall be based on the Committee's assessment of Drax's performance for the preceding year.
- The Committee's assessment of Drax's annual performance will be based on: i) actual results against the Company's Business Plan; and ii) Drax's total shareholder return against a peer group initially comprising the FTSE 250.

3. A Savings Related Share Option Plan ("SAYE plan") approved by HM Revenue & Customs under which participation must be offered on similar terms to all UK resident employees (including executive directors) of the Group who have been employed for such period (not exceeding five years) as may be specified by the Remuneration Committee when making invitations. The scheme allows the amount payable on maturity of three and/or five year savings contracts with an approved provider (Yorkshire Building Society) to be invested by each participant in a number of ordinary shares determined by reference to: i) the price of ordinary shares at the date of entering into the savings contract; ii) the amount the participant contracts to save (which must not exceed £250 per month); and iii) a discount, determined by the Committee and not exceeding 20%, to the price of a share (determined in accordance with the rules of the scheme).

It is the Committee's intention to launch the SAYE scheme shortly and that all employees should be offered the opportunity to participate with options being granted at a 20% discount.

PROPORTIONS OF 2005 AND EXPECTED PROPORTIONS OF FUTURE ANNUAL REMUNERATION PACKAGE FOR EXECUTIVE DIRECTORS

The LTIP matured as a result of the Refinancing and Listing in December 2005. Consequently, executive directors and all other Drax employees received a significant proportion of their total rewards for that year in the form of shares and cash payable by virtue of the LTIP. The proportion varied between directors as is evident from the tables in Part 2 of this report.

Remuneration Report continued

Assuming "on target" Company performance and ignoring benefits in kind, car allowances and benefits from the SIP and SAYE scheme, until ESIP awards (not yet made) mature, variable pay for executive directors will amount to approximately 25% of the total of base and variable pay (including pension contributions).

As the ESIP has not yet been implemented, it is not appropriate to forecast relative proportions of remuneration when the first and subsequent ESIP cycles vest.

SERVICE AGREEMENTS FOR DIRECTORS

The Committee's policy is that executive directors' service agreements should be of indefinite duration subject to a normal retirement age of 63 and terminable at any time by the Company giving 12 months' prior notice and by the executive director giving six months' prior notice. In order to recruit and retain specific individuals, this policy has been varied in the following respects:

With effect from admission and for a period of two years thereafter Dorothy Thompson's service agreement is terminable by either party on not less than 12 months' notice in writing and thereafter by giving a period of six months' notice in writing.

In the event of a change of control within 12 months of the date of commencement, Dorothy Thompson would be entitled to the following less £923,670 (being the value of her LTIP awards):

- (a) a sum equivalent to the Basic Annual Salary (as at the Termination Date) for a period of 18 months;
- (b) a payment reflecting loss of expectation of a bonus based on achieving the performance targets for a period of 18 months and amounting to 40% of basic annual salary; and
- (c) a payment of £54,000 by way of compensation in respect of loss of the executive's contractual benefits in kind.

Such payments would be inclusive of any payment in lieu of notice due to Dorothy Thompson on termination.

Pursuant to each of the executive directors' service agreements, Drax 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.

The following table shows for each person who has served as a director of the Company or of Drax Group Limited at any time during the year ended 31 December 2005, the date of the service agreement or contract for services, the unexpired term and details of the notice periods together with any provisions for compensation payable upon early termination.

	Contract start date	Unexpired term	Notice period by the Company	Notice period by the director	Compensation payable upon early termination
Gordon Horsfield ⁽¹⁾	07.03.2006	Indefinite duration	6 months	6 months	Not fixed by the agreement
Tim Barker	30.06.2004	"	1 month	1 month	"
Charles Berry ⁽²⁾	15.12.2005	"	1 month	1 month	"
Jamie Dundas ⁽²⁾	15.12.2005	"	1 month	1 month	"
Mike Grasby	22.12.2003	"	1 month	1 month	"
Dorothy Thompson ⁽³⁾	26.09.2005	"	(3)	(3)	"
Peter Emery	14.06.2004	"	12 months	6 months	"
Gordon Boyd	10.01.2005	"	12 months	6 months	"

(1) At 31 December 2005 Gordon Horsfield was employed under a service agreement dated 19 December 2003 terminable by either party on six months' notice. That agreement was terminated, at no cost to the Group, upon Gordon Horsfield relinquishing his executive responsibilities on 7 March 2006.

(2) Neither Charles Berry nor Jamie Dundas served as directors of Drax Group Limited. Each became a director of the Company on 15 December 2005.

(3) See the description of the termination provisions earlier in this section of the report.

(4) Gerald Wingrove was appointed as Chief Executive pursuant to a service agreement dated 19 December 2003 which provided for termination by the Company upon 12 months' notice and by Mr Wingrove on at least six months' notice. He ceased to be a director of the group by mutual consent on 19 April 2005 and ceased employment with the group by mutual consent on 31 May 2005. The payment made to him at the time of his departure is shown in the table of emoluments in Part 2 of this report.

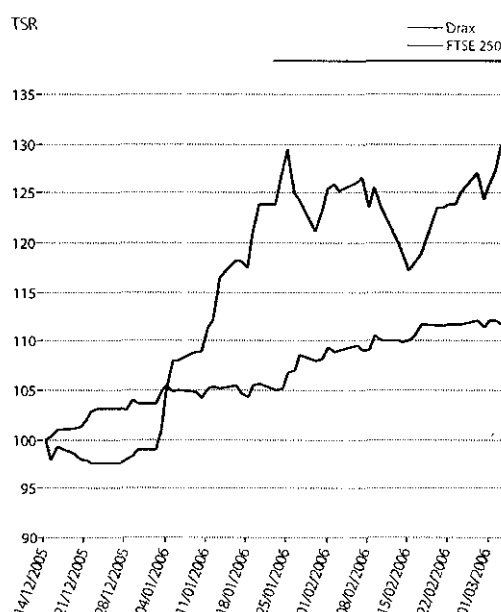
Directors' service agreements and contracts for services are available for inspection at the Company's registered office during normal hours of business and will be available at the place of the Annual General Meeting from 10am until the close of the meeting.

EXTERNAL APPOINTMENTS

The Committee recognises that executive directors may be invited to become non-executive directors of other companies, and that such appointments can broaden their knowledge and experience to the benefit of the Company. No executive director currently holds a directorship of any other company in respect of which he receives a fee for his services but it is the Committee's policy that the individual director would be entitled to retain the fees in respect of any appointment approved in advance by the Committee.

SHARE PERFORMANCE

The Company was introduced to the Official List of the UK Listing Authority and its shares admitted to trading on the London Stock Exchange on 15 December 2005 ("Listing"), 16 elapsed days (10 business days) before the end of the financial year on 31 December 2005. The Company has not yet made any distributions to shareholders. The graph opposite shows movements in the Company's share price relative to total shareholder return ("TSR") for the FTSE 250 index between Listing and 1 March 2006. The FTSE 250 has been chosen as the comparator because the Company's market capitalisation is comparable with the market capitalisations of the larger companies within that index. The price of an ordinary share in the Company at the start of trading on 15 December 2005 was £5.00 and the closing price on the last day of the year upon which the Company's shares were traded (30 December 2005) was £4.95.

**Part 2: Audited Information**

This section of the report (which has been subject to audit) sets out the remuneration paid to the directors during the year to 31 December 2005.

1 DIRECTORS' EMOLUMENTS

The emoluments payable in respect of 2005 to directors who held office for any part of the financial year, including amounts paid to them as directors of subsidiary undertakings and compensation for loss of office, was as follows:

	Salary £'000	Fees ⁽¹⁾ £'000	Additional fees ⁽²⁾ £'000	Cash bonus in respect of 2005 £'000	Benefits ⁽³⁾ £'000	Pension ⁽⁴⁾ £'000	Termination payment £'000	Total 2005 £'000	Total 2004 ⁽⁵⁾ £'000
Gordon Horsfield	262	-	-	147	17	52	-	478	863
Tim Barker	-	46	88	-	-	-	-	134	28
Charles Berry	-	7	-	-	-	-	-	7	n/a
Jamie Dundas	-	7	-	-	-	-	-	7	n/a
Mike Grasby	-	51	80	-	-	-	-	131	52
Dorothy Thompson	92	-	-	48	11	18	-	169	n/a
Peter Emery	170	-	-	89	91	34	-	384	159
Gordon Boyd ⁽⁶⁾	185	-	-	104	25	37	-	351	n/a
Gerald Wingrove ⁽⁷⁾	123	-	-	-	11	25	469	628	870

(1) Includes Board Committee membership fees and, for Charles Berry and Jamie Dundas, a one-off familiarisation process fee of £5,000.

(2) Paid after the end of the financial year in respect of significant additional time spent on the affairs of the Group in 2005 and calculated on the basis of time spent, as explained in Part 1 of the report.

(3) Includes relocation assistance of £73,000 for Peter Emery, £6,000 for Gordon Boyd and £5,000 for Dorothy Thompson.

(4) Annual contribution by the Company to director's pension plan or cash in lieu.

(5) In respect of 2004 emoluments:

- (a) Gordon Horsfield and Gerald Wingrove received a restructuring bonus of £400,000 each.
- (b) Peter Emery was appointed to the Board as Production Director on 14 June 2004.
- (c) Tim Barker was appointed to the Board on 30 June 2004.

(6) Gordon Boyd was appointed to the Board as Finance Director on 10 January 2005.

(7) Gerald Wingrove ceased to be a director on 19 April 2005 and his service agreement terminated on 31 May 2005, in both cases by mutual consent.

Remuneration Report continued

DIRECTORS' INTERESTS IN THE DRAX GROUP LONG-TERM INCENTIVE PLAN

The following table shows particulars of the directors' interests during 2005 in the LTIP established by Drax Group Limited ("DGL") in May 2004. Further details of the Plan are given in note 21 to the Consolidated Financial Statements on pages 63 to 65. DGL was the holding company of the group until Listing.

Under the LTIP, two types of points (one type giving a conditional right to cash and the other a conditional right to non-voting shares in DGL) were allocated on the various dates shown in the table. In the events which transpired, the only condition to the vesting of the conditional rights conferred by the points which proved to be of relevance was the Listing.

The absence of a market for non-voting shares in DGL and the way in which the rules of the LTIP operated meant that the earliest time at which a value could be attributed to the points awarded was upon Listing when the points held by each individual converted to a right to a proportionate share (according to the individual's points and the total number of points then held by all beneficiaries) of £5.1m in cash and of a number of shares in DGL which, upon Listing, were exchanged (at the rate of three shares in the Company for one share in DGL) for a total of 11,321,031 shares in the Company.

The table below shows cash and numbers of shares in the Company, not in DGL. The total value (whether in cash or shares) received upon or (in the case of cash) receivable in consequence of Listing by an individual and by virtue of points awards has been apportioned to award dates, rateably according to the proportion of the individual's total points which were awarded to him or her on each award date.

In addition to points awards, the rules of the LTIP provided for "Initial Awards" which entitled the selected beneficiaries of the awards to buy non-voting shares in DGL in May 2004 at a price of 13.65 pence per DGL share. In the table, those Initial Awards are shown as shares held at 1 January 2005 and the numbers given are the numbers of shares in the Company equivalent to the DGL shares purchased.

For completeness, the table below includes particulars of the shares in the Company acquired by Gordon Horsfield and Gerald Wingrove upon Listing by exchange of the non-voting shares in DGL which each of them acquired in May 2004 as a result of investing the restructuring bonuses awarded to each of them by resolution of the shareholders of DGL passed on 30 April 2004.

Upon Listing:

- (a) By virtue of: i) the cash to which points awards gave a right; and ii) the exchange of the DGL shares to which points awarded gave a right, each director became absolutely entitled to the shares in the Company and to receive one half of the cash shown in the column headed "Total benefits derived from points awards under the LTIP". Entitlement to receive the other half of the cash sum is conditional upon the individual being in the service of the Group on 15 December 2006 or having left the service of the Group in circumstances where the "good leaver" provisions of the LTIP apply.
- (b) All scheme interests vested within the meaning of Schedule 7A of the Companies Act 1985 when the price of an ordinary share in the Company was £5.00.

The Committee has established the ESIP as a long-term incentive plan to replace the LTIP but no awards have yet been made pursuant to it nor have all the conditions attaching to awards yet been finally determined. The Committee's intentions are stated in Part 1 of this report.

	Restructuring bonus shares (not awarded under the LTIP)	Shares held at 01/01/05 (Initial Award)	Type of award	By virtue of points awarded prior to 01/01/05	By virtue of points awarded on 17/01/05	By virtue of points awarded on 13/06/05	By virtue of points awarded on 19/09/05	Total benefits derived from awards under the LTIP
Gordon Horsfield	5,188,320	349,212	Shares	-	261,719	-	854,032	1,464,963
			Cash	£137,700	£96,900	-	£306,000	£540,600
Gerald Wingrove ⁽¹⁾	5,188,320	236,976	Shares	-	-	-	-	236,976
			Cash	£91,800	-	-	-	£91,800
Peter Emery	-	-	Shares	-	231,961	-	504,857	736,818
			Cash	-	£86,700	-	£270,300	£357,000
Gordon Boyd ⁽²⁾	-	-	Shares	-	-	231,961	504,857	736,818
			Cash	-	-	£86,700	£270,300	£357,000
Dorothy Thompson ⁽³⁾	-	-	Shares	-	-	-	168,414	168,414
			Cash	-	-	-	£81,600	£81,600

(1) Gerald Wingrove was a director of DGL and of its subsidiaries until 19 April 2005. His service agreement with Drax Power Limited came to an end on 31 May 2005. As a consequence of him no longer being in the service of the group, Mr Wingrove ceased to have the benefit of points conditionally awarded in January 2005 but retained his interest in the Initial Award which, in common with all other Initial Awards, ceased to be conditional upon his employment by the group continuing beyond December 2004.

(2) Gordon Boyd joined the group on 10 January 2005.

(3) Dorothy Thompson joined the group on 26 September 2005.

DIRECTORS' INTERESTS IN DRAX GROUP SHARES

The interests held by each person who was a director at the end of the financial year in the ordinary shares of 10 pence each in the Company are shown below. Where details are given at a date prior to Listing, the interest held has been converted from a number of shares in DGL to a number of shares in the Company by applying the exchange rate of three shares in the Company for every one share in DGL which applied to all DGL shareholdings at Listing. All the disclosed interests are beneficial. The value of shares received on 15 December 2005 in consequence of the award of points under the LTIP was subject to income tax and employees' national insurance contributions payable by the recipient of the shares. On 15 December 2005 each recipient sold at least sufficient of the shares so received to satisfy those tax and national insurance liabilities.

	Shares held at 01/01/05	Shares in the Company received on 15/12/05 by virtue of points awards under the LTIP	Shares sold at £5 per share on 15/12/05	Shares acquired on or after 15/12/05 but before 31/12/05	Shares held at 31/12/05
Gordon Horsfield	5,537,532	1,115,751	1,697,458	-	4,955,825
Dorothy Thompson ⁽¹⁾	-	168,414	69,049	-	99,365
Peter Emery	-	736,818	519,456	-	217,362
Gordon Boyd	-	736,818	519,456	-	217,362
Tim Barker	-	-	-	4,000	4,000
Charles Berry ⁽²⁾	-	-	-	-	-
Jamie Dundas ⁽²⁾	-	-	-	-	-
Mike Grasby	-	-	-	-	-

(1) On 4 January 2006, Dorothy Thompson disposed of 48,000 shares. No other change to directors' interests has been notified to the Company between the end of the financial year on 31 December 2005 and the date this report was approved by the Board.

(2) Charles Berry and Jamie Dundas became directors upon Listing on 15 December 2005.

(3) Gerald Wingrove ceased to be a director of Drax Group Limited and its subsidiaries on 19 April 2005. He held as shares in Drax Group Limited the equivalent of 5,425,296 shares in the Company at the date of leaving the group's service.

This report was reviewed and approved by the Board on 7 March 2006.



Tim Barker
Chairman
Remuneration Committee

Independent Auditors' Report

To the Members of Drax Group plc

We have audited the group financial statements of Drax Group plc for the year ended 31 December 2005 which comprise the consolidated income statements, the consolidated statements of recognised income and expense, the consolidated balance sheets, the consolidated cash flow statements and the related notes 1 to 34. These group financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the directors' remuneration report that is described as having been audited.

We have reported separately on the individual company financial statements of Drax Group plc for the period ended 31 December 2005.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of Directors and Auditors

The directors' responsibilities for preparing the annual report, the directors' remuneration report and the group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted for use in the European Union are set out in the statement of directors' responsibilities.

Our responsibility is to audit the group financial statements and the part of the directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the group financial statements give a true and fair view in accordance with the relevant financial reporting framework and whether the group financial statements and the part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We report to you if, in our opinion, the directors' report is not consistent with the group financial statements. We also report to you if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' transactions with the company and other members of the group is not disclosed.

We also report to you if, in our opinion, the company has not complied with any of the four directors' remuneration disclosure requirements specified for our review by the Listing Rules of the Financial Services Authority. These comprise the amount of each element in the remuneration package and information on share options, details of long term incentive schemes, and money purchase and defined benefit schemes. We give a statement, to the extent possible, of details of any non-compliance.

We review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services

Authority, and we report if it does not. We are not required to consider whether the board's statement on internal control covers all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section including the unaudited part of the directors' remuneration report and we consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the group financial statements.

Basis of Audit Opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the group financial statements and the part of the directors' remuneration report described as having been audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the group financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted for use in the European Union, of the state of the group's affairs as at 31 December 2005 and of its profit for the year then ended; and
- the group financial statements and the part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

Deloitte & Touche LLP

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors
London
7 March 2006

Consolidated Income Statements

	Notes	Years ended 31 December	
		2005 £'m	2004 £'m
Continuing operations			
Revenue		928.6	624.1
Fuel costs		(539.5)	(384.7)
Other operating expenses excluding exceptional items	6	(180.9)	(186.9)
Other exceptional operating income	5	329.9	–
Other exceptional operating expenses	5	(66.6)	–
Total other operating income / (expenses)		82.4	(186.9)
Other income		–	2.5
Unrealised losses on derivative contracts	18	(117.0)	–
Operating profit	6	354.5	55.0
Interest payable and similar charges	7	(114.4)	(101.2)
Interest receivable	7	23.5	4.6
Profit / (loss) before tax		263.6	(41.6)
Tax credit	8	18.8	35.1
Profit / (loss) for the year attributable to equity shareholders from continuing operations		282.4	(6.5)
Earnings per share from continuing operations expressed in pence per share			
– Basic and diluted	9	98.0	(2.4)

The results above relate to the continuing operations of the Group.

Consolidated Statements of Recognised Income and Expense

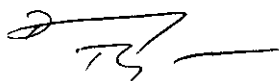
	Years ended 31 December		
	Notes	2005 £'m	2004 £'m
Profit / (loss) for the year		282.4	(6.5)
Actuarial losses on defined benefit pension schemes	30	(8.2)	(6.1)
Deferred tax on actuarial losses on defined benefit pension schemes	8	2.5	1.8
Initial recognition of net mark-to-market liability on adoption of IAS 32 and IAS 39	18	(5.6)	–
Deferred tax recognised on adoption of IAS 32 and IAS 39	8	1.7	–
Fair value losses on cash flow hedges	18	(109.7)	–
Deferred tax recognised on fair value losses on cash flow hedges	8	32.9	–
Net losses not recognised in income statement		(86.4)	(4.3)
Total recognised income / (expense) for the year attributable to equity shareholders		196.0	(10.8)

Consolidated Balance Sheets

	As at 31 December		
	Notes	2005 £m	2004 £m
Assets			
Non-current assets			
Property, plant and equipment	11	1,050.5	1,037.7
Derivative financial instruments	18	0.3	-
		1,050.8	1,037.7
Current assets			
Inventories	12	67.8	45.2
Trade and other receivables	13	192.9	69.5
Derivative financial instruments	18	7.7	-
Cash at bank and in hand	14	99.1	75.7
		367.5	190.4
Liabilities			
Current liabilities			
Financial liabilities:			
- Borrowings	16	101.4	204.7
- Derivative financial instruments	18	173.0	-
Trade and other payables	15	176.1	66.9
Current tax liabilities		5.2	2.5
		455.7	274.1
		(88.2)	(83.7)
Net current liabilities			
Non-current liabilities			
Financial liabilities:			
- Borrowings	16	460.1	1,078.6
- Derivative financial instruments	18	49.6	-
Deferred tax liabilities	20	185.3	246.7
Retirement benefit obligations	30	44.7	36.5
Other non-current liabilities	17	0.7	25.8
Provisions	19	2.0	0.5
		742.4	1,388.1
		220.2	(434.1)
Net assets / (liabilities)			
Shareholders' equity			
Issued equity	22	40.7	-
Share premium	27	420.7	0.5
Merger reserve	23	710.8	445.1
Capital reserve	24	-	293.5
Hedge reserve	25	(76.8)	-
Retained losses	26	(875.2)	(1,173.2)
Total shareholders' equity	27	220.2	(434.1)

These financial statements were approved by the Board of directors on 7 March 2006.

Signed on behalf of the Board of directors.



Dorothy Thompson
Chief Executive



Gordon Boyd
Finance Director

Consolidated Cash Flow Statements

	Years ended 31 December		
	Notes	2005 £'m	2004 £'m
Cash generated from operations	28	462.3	73.4
Income taxes paid		(2.8)	(0.4)
Decrease in restricted cash		26.9	16.9
Interest paid prior to the Refinancing and Listing		(57.5)	(77.4)
Interest paid on the Refinancing and Listing	16	(86.2)	-
Interest received		5.8	4.6
Net cash generated from operating activities		348.5	17.1
Cash flows from investing activities			
Purchase of property, plant and equipment		(25.0)	(13.7)
Net cash used in investing activities		(25.0)	(13.7)
Cash flows from financing activities			
Repayment of borrowings prior to the Refinancing and Listing	16	(267.6)	-
Repayment of borrowings on the Refinancing and Listing	16	(582.6)	-
Debt issued as a result of the Refinancing and Listing	16	577.0	-
Net proceeds on issue of ordinary share capital		-	0.5
Net cash (used in) / generated from financing activities		(273.2)	0.5
Net increase in cash and cash equivalents		50.3	3.9
Cash and cash equivalents at beginning of the period	14	37.5	33.6
Cash and cash equivalents at end of the period	14	87.8	37.5

Notes to the Consolidated Financial Statements

1. General Information

Drax Group plc (the "Company") is a company incorporated in England and Wales under the Companies Act 1985. Drax Group plc and its subsidiaries (together the "Group") operate in the electricity generation industry within the UK. The address of Drax Group plc's registered office and principal establishment is Drax Power Station, Selby, North Yorkshire, YO8 8PQ, United Kingdom. The operating companies of the Group are disclosed within note 3 of the Company's separate financial statements, which follow these consolidated financial statements.

2. Basis of Preparation

The financial statements have been prepared on the basis of all applicable International Financial Reporting Standards ("IFRS") including all International Accounting Standards ("IAS"), and all applicable Standing Interpretations Committee ("SIC") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations issued by the International Accounting Standards Board ("IASB") and endorsed by the EU.

The Group's date of transition to IFRS is 1 January 2002, being the beginning of the period for which historical consolidated IFRS financial information was prepared for the Prospectus issued pursuant to the Group's introduction to the Official List of the UK Listing Authority and to the trading of Drax Group plc ordinary shares on the London Stock Exchange.

The financial statements are the first prepared by the Group in accordance with accounting standards as adopted for use in the EU and as such take account of the requirements and options in IFRS 1 "First-time Adoption of International Financial Reporting Standards" as they relate to the comparative financial information.

Note 3 below sets out how, in preparing these financial statements, the directors have applied accounting standards as adopted for use in the EU under the first-time adoption provisions set out in IFRS 1. Certain of the requirements and options in IFRS 1 relating to comparative financial information presented on first-time adoption may result in a different application of accounting policies in the financial information for the year ended 31 December 2004 to that which would apply if those were the first financial statements of the Group prepared in accordance with accounting standards as adopted for use in the EU. In particular, in accordance with the transitional arrangements set out in IFRS 1, Drax Group plc has elected not to restate the comparative financial information to show the effect of IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement" and, as a consequence, for the year ended 31 December 2004, financial instruments continue to be accounted for in accordance with the Group's previous policies for financial instruments under UK Generally Accepted Accounting Principles ("UK GAAP"). In contrast, for the year ended 31 December 2005, IAS 32 and IAS 39 have been applied. This is further explained in notes 3(a), 3(r) and 3(s) below.

The financial statements have been prepared under the historical cost convention basis as modified by the revaluation of financial assets and liabilities following the application of IAS 39 from 1 January 2005.

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective:

IFRS 6	Exploration for and Evaluation of Mineral Resources
IFRS 7	Financial Instruments: Disclosures; and the Related Amendment to IAS 1 on Capital Disclosures
IFRIC 4	Determining Whether an Arrangement Contains a Lease
IFRIC 5	Rights to Interest Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds

The directors anticipate that the adoption of the Standards and Interpretations in future periods will have no material impact on the financial statements of the Group, except for additional disclosures on capital and financial instruments when the relevant standards come into effect for periods commencing on or after 1 January 2007.

3. Summary of Significant Accounting Policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to both years presented, unless otherwise stated.

(A) IFRS 1 EXEMPTIONS

The Group's date of transition to IFRS is 1 January 2002. On transition to IFRS, the Group has taken advantage of the following exemptions to assist groups with the transition process contained within IFRS 1:

- Business combinations: the Group has elected to allow business combinations which were effected before the IFRS transition date to be exempted from restatement under IFRS 3 "Business Combinations".
- Employee benefits: the cumulative actuarial losses relating to pensions and other post retirement benefits at the date of transition to IFRS have been recognised in retained earnings.
- Cumulative translation reserve: the Group has elected to reset the translation reserve to zero at the date of transition to IFRS.
- Share-based payment: the Group has only applied IFRS 2 "Share-based Payment" to equity instruments granted after Exposure Draft 2 "Share-based Payment" was issued on 7 November 2002 and that have not vested by 31 December 2004.
- Financial instruments: the Group has elected not to prepare comparative financial information for the year ended 31 December 2004 in accordance with IAS 32 and IAS 39. These standards have been applied with effect from 1 January 2005. The Group has continued to use its previous UK GAAP accounting policy in preparing the financial information for the year ended 31 December 2004.

(B) PRINCIPLES UNDERLYING GOING CONCERN ASSUMPTION

The financial statements have been prepared on the going concern basis in accordance with IAS 1 "Presentation of Financial Statements". The directors believe this to be appropriate and consistent with the Group's cash flow and profit forecasts, which evidence the Group's long-term profitability.

If for any reason Drax Group plc is unable to meet its financial obligations as they fall due the Company may have to take appropriate insolvency proceedings and cease to be a going concern, in which case adjustment may have to be made to reduce the monetary values of assets to the recoverable amounts, to provide for further liabilities that might arise and to reclassify the non-current assets and liabilities as current assets and liabilities.

(C) BASIS OF CONSOLIDATION

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company made up to the reporting date each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of the acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. Any deficiency in the cost of acquisition below the fair values of the identifiable net assets acquired (discount on acquisition) is credited to the income statement in the period of acquisition. The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies into line with those used by the Group.

All intra-Group transactions, balances, income and expenses are eliminated on consolidation.

The Group underwent a financial restructuring (the "Refinancing and Listing") effective on 15 December 2005 which resulted in the creation of a new holding company, Drax Group plc. Pursuant to the schemes of arrangement under which the Refinancing and Listing was implemented,

Notes to the Consolidated Financial Statements continued

the existing debt of the Group was settled, partially through the issue of new debt and partially through the issue of ordinary shares in Drax Group plc. Also on 15 December 2005, Drax Group plc was introduced to the Official List of the UK Listing Authority and its ordinary shares commenced trading on the London Stock Exchange.

Under IFRS 3, the insertion of Drax Group plc as the new holding company has been accounted for as a reverse acquisition, whereby Drax Group Limited (being the previous Group holding company), the legal subsidiary, acquired Drax Group plc, the legal parent company. The impact of the Refinancing and Listing on the Group's debt and share capital is illustrated in notes 16 and 22 respectively.

(D) USE OF ESTIMATES

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's reasonable knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Fixed assets and depreciation – Estimated remaining useful lives and residual values are reviewed annually, taking into account prices prevailing at each balance sheet date. The carrying values of fixed assets are also reviewed for impairment where there has been a trigger event 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 the directors' reasonable estimates of future prices, output and costs, and is therefore subjective.

Pensions – Within the UK, the Group principally operates an approved defined benefit scheme. The Group accounts for this scheme in accordance with IAS 19 with the cost of providing benefits determined using the projected unit credit method, and actuarial valuations being carried out at each balance sheet date. Inherent in these valuations are key assumptions, including discount rates, expected returns on plan assets and salary and pension increases. These actuarial assumptions are reviewed annually and modified as appropriate. The Group believes that the assumptions utilised in recording 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.

Emissions allowances – Liabilities in respect of obligations to deliver emissions allowances are recognised as incurred by reference to generation for the period. Any liabilities recognised are measured based on the current estimates of the amounts that will be required to satisfy the net obligation taking into account the market price of emissions allowances at the balance sheet date. The actual cost of those allowances not already acquired may be different and the number of allowances may be different, as actual generation may not be the same as expected generation.

Deferred taxation – Full provision is made for deferred taxation, as required under IAS 12 "Income Taxes", at the rates of tax prevailing at the period end dates unless future rates have been substantively enacted. Deferred tax assets are recognised where it is more likely than not that they will be recovered.

Derivatives – The Group has applied IAS 32 and IAS 39 from 1 January 2005. IAS 39 requires derivative financial instruments to be recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in earnings unless specific hedge accounting criteria are met. The fair values of derivative instruments for commodities 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 at future dates. The Group generally bases its forward price curves upon readily obtainable market

price quotations, as the Group's commodity 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.

(E) REVENUE RECOGNITION

Revenue represents amounts receivable for goods and services provided in the normal course of business, net of trade discounts, VAT and other sales related taxes and excluding transactions with or between wholly-owned subsidiaries.

Revenues from the sale of electricity are recorded based upon output delivered at rates specified under contract terms or prevailing market rates as applicable.

Revenues from sales of Renewables Obligation Certificates are recorded at the invoiced value, net of VAT. Revenue is recognised at the point there is a binding agreement to sell.

Where goods or services are exchanged for goods or services of a similar nature and value, the exchange is not treated as giving rise to revenue. Where goods or services are exchanged for goods or services of a dissimilar nature, the exchange is treated as giving rise to revenue. The revenue is measured at the fair value of goods or services received, adjusted by the amount of any cash or cash equivalents received or paid. If the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up, adjusted by the amount of any cash or cash equivalents received or paid.

(F) SEGMENTAL REPORTING

Turnover comprises primarily sales of electricity generated by the Group to the electricity wholesale market in England and Wales. As such, the Group has only one business segment and one geographical segment.

(G) GOODWILL

Goodwill represents the excess of the fair value of the purchase consideration over the Group's share of the fair value of the identifiable assets and liabilities of an acquired business at the date of acquisition.

Goodwill is recognised as an asset and reviewed for impairment at least annually and whenever there is an indication of impairment. Goodwill is carried at cost less amortisation charged prior to the Group's transition to IFRS on 1 January 2002 less accumulated impairment losses. Any impairment is recognised in the period in which it is identified.

(H) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is 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 initial estimate of costs of dismantling and removing the item and restoring the site. Property, plant and equipment is stated at cost less accumulated depreciation and any provision for impairment in value. Freehold land and assets in the course of construction are not depreciated. Depreciation is provided on a straight line basis to write-down assets to their residual value evenly over the estimated useful lives of the assets from the date of acquisition by the Group. The estimated remaining useful lives are:

	Years
Freehold buildings, plant and machinery	4-40
Decommissioning asset	35
Plant spare parts	35

Estimated remaining useful lives and residual values are reviewed annually,

taking into account commercial and technological obsolescence as well as normal wear and tear, and any provision for impairment calculated in accordance with IAS 36 "Impairment of Assets". Residual values are based on prices prevailing at each balance sheet date.

Subsequent costs relating to major inspections and overhauls of the station are included in the asset's carrying amount or recognised as a separate asset, as appropriate, if the recognition criteria of IAS 16 "Property, Plant and Equipment" 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.

(I) IMPAIRMENT OF TANGIBLE ASSETS

At each balance sheet date, the Group reviews its tangible assets to determine whether there is any indication that these assets may have suffered an impairment loss. If such an indication exists, the recoverable amount is assessed by reference to the net present value of expected future cash flows of the asset (value-in-use) or fair value less selling costs, if higher. If an asset is impaired, a provision is made to reduce its carrying amount to the estimated recoverable amount. The discount rate applied is a pre-tax rate based upon the Group's weighted average cost of capital and reflects the current market assessment of the time value of money and the risks specific to the business.

During the year to 31 December 2002, the Group performed an impairment review following the loss of a long-term power purchase agreement with TXU Europe Energy Limited (the "TXU Hedging Contract") and its related income streams. This resulted in the write down of goodwill to nil, and a provision for impairment of £20.4 million against tangible fixed assets, to write down the assets to their estimated recoverable amount.

In accordance with IAS 36, the Group assessed at each subsequent reporting date whether there was any indication that the impairment loss recognised at 31 December 2002 should be reversed. As a result of the assessment performed at 30 June 2005 for the purposes of the financial information prepared in connection with the Refinancing and Listing, which highlighted significant increases in wholesale electricity prices that the Group has been able to achieve in its forward contractual position, the Group recorded a reversal of the tangible fixed asset impairment of £19.0 million. This represents a reversal of the total impairment loss recognised at 31 December 2002 after adjusting for depreciation.

(J) DECOMMISSIONING COSTS

Provision is made for the estimated decommissioning costs at the end of the useful economic life of the Group's generating assets, if and when a legal or constructive obligation arises, on a discounted basis. The amount provided represents the present value of the expected costs. An amount equivalent to the initial provision is capitalised within tangible fixed assets and is depreciated over the useful lives of the related assets. The unwinding of the discount is included in interest payable and similar charges.

(K) INVENTORIES

Operating stocks of fuel and consumables are valued at the lower of average cost and net realisable value.

The Group is able to claim Renewables Obligation Certificates ("ROCs") from the Office of Gas and Electricity Markets ("OFGEM") as a result of burning renewable fuels. A market exists for sale of ROCs and the Group recognises income in the income statement at the point where there is a binding agreement to sell ROCs to a third party which transfers the risks and rewards of ownership. The attributable incremental cost of generating ROCs above that of burning coal is included within inventory in respect of ROCs earned but not yet sold and is recognised in the income statement only as sales of ROCs are recorded. The inventory value is stated at the lower of cost and net realisable value.

(L) EMISSIONS ALLOWANCES

The Group recognises its free emissions allowances received under the National Allocation Plan at nil cost. Any additional allowances purchased in the market are recorded at cost. The Group also recognises a liability in respect of its obligations to deliver emissions allowances. The charge to the income statement and the related liability is measured based on the current estimates of the amounts that will be required to satisfy the net obligation, taking into account free allowances allocated under the National Allocation Plan, market purchases and forward contracts already in place.

This accounting policy is consistent with the Group's accounting policy previously applied under UK GAAP. It does not reflect the accounting rules contained within IFRIC 3 "Emission Rights", as IFRIC 3 was withdrawn by the International Accounting Standards Board in June 2005.

(M) TAXATION

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 the difference between the carrying amounts of assets and liabilities in the balance sheet and the corresponding tax bases used in the computation of taxable profits, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profit 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 in which the liability is settled or the asset is realised, and is charged in the income statement, except where it relates to items charged or credited to equity via the statement of recognised income and expense, in which case the deferred tax is also dealt with in equity and is shown in the statement of recognised income and expense.

(N) LEASED ASSETS

The Group has no significant commitments under operating or finance lease agreements.

(O) PENSION AND OTHER POST RETIREMENT BENEFITS

The Group provides pensions through an approved industry defined benefit scheme and a defined contribution scheme. The cost of providing benefits under the defined benefit scheme is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. The Group has taken advantage of the additional option within the Amendment to IAS 19 "Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures", to recognise all actuarial gains and losses in the period in which they occur outside the income statement in the statement of recognised income and expense.

The current service cost element of the pension charge is deducted in arriving at operating profit. The retirement benefits obligation recognised in the balance sheet represents the net deficit in the Group's defined benefit pension scheme, gross of deferred tax.

For the defined contribution scheme, the Group pays contributions to publicly or privately administered pension insurance plans on a mandatory, contractual or voluntary basis. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due to be paid.

(P) SHARE-BASED PAYMENT

The Group has taken advantage of the IFRS 1 exemption to only apply IFRS 2 to awards granted since Exposure Draft 2 was issued on 7 November 2002, and which have not vested by 31 December 2004. Share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of share-based payments is expensed on a straight-line basis over the vesting period, based on an estimate of the shares that will

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ultimately vest. The fair value of share-based payments under the Group's Long-Term Incentive Plan (the "LTIP") has been calculated based on the fair value of the equity at the date of grant (note 21).

(Q) FOREIGN CURRENCIES

The Group's consolidated financial statements are presented in sterling, which is the functional and presentational currency of the Company and its principal subsidiaries.

Transactions in foreign currencies are translated into the functional currencies of individual entities at the exchange rate ruling at the date of transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the exchange rate ruling at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

(R) FINANCIAL INSTRUMENTS (UK GAAP POLICIES APPLIED IN THE PREPARATION OF THE CONSOLIDATED IFRS FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2004)

The accounting policies below, which have been applied in preparing the IFRS financial statements for the year ended 31 December 2004, are those policies applied by the Group under UK GAAP for the year then ended. The Group has adopted revised accounting policies for financial instruments from 1 January 2005, the date of implementation of IAS 32 and IAS 39. These revised policies are detailed in note 3(S) below.

The Group uses a range of derivative instruments, including interest rate swaps, energy-based futures contracts and foreign exchange contracts for hedging purposes.

Debt instruments – All borrowings are stated at the fair value of consideration received after deduction of issue costs. The issue costs and interest payable on debt instruments are charged to the income statement at a constant rate over the life of the instruments.

Interest rate swaps – These are used to manage debt interest rate exposures. Amounts payable or receivable in respect of these agreements are recognised as adjustments to interest expense over the period of the contracts.

Forward contracts – The Group enters into forward contracts for the purchase and / or sale of foreign currencies in order to manage its exposure to fluctuations in currency rates. The cash flows from forward purchase contracts are classified in a manner consistent with the underlying nature of the hedged transaction. Hence unrealised gains and losses on contracts hedging forecast transactions are not accounted for until the maturity of the contract. Foreign currency debtors and creditors that are hedged are translated at the exchange rate ruling at the balance sheet date. All energy-based futures contracts are accrual accounted as hedges of future generation.

Interest differentials on derivative instruments are charged to the income statement as interest costs in the period to which they relate.

(S) FINANCIAL INSTRUMENTS (IFRS POLICIES APPLIED IN THE PREPARATION OF THE CONSOLIDATED IFRS FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2005)

The Group has applied IAS 32 and IAS 39 in the financial year beginning 1 January 2005. In accordance with the transitional arrangements set out in IFRS 1, the Group has not restated the prior year's comparative figures to show the effect of IAS 32 and IAS 39. For the year ended 31 December 2004, financial instruments continue to be accounted for in accordance with the Group's previous policies for financial instruments under UK GAAP, as set out in note 3(R) above.

IAS 39 requires that all financial assets and liabilities be measured at fair value in the balance sheet with changes in fair value reported through the income statement, or the hedge reserve to the extent that contracts are considered effective hedges.

Derivative instruments, and commodity contracts that fall within the scope of IAS 39, are carried at fair value with specific rules applying to all financial instruments which form part of a hedging relationship.

IAS 32 prescribes certain disclosures on the use and impact of financial instruments designed to help the users of accounts understand the significance of the financial instruments to an entity's financial position, performance and cash flows, as well as the factors that affect amounts, timing and risks associated with future cash flows.

Financial liability and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences residual interest in the assets of the Group after deducting all of its liabilities.

Debt instruments – The Group measures all debt instruments, whether financial assets or financial liabilities, initially at fair value of the consideration paid or received. 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, in effect, amortised through the income statement over the life of the instrument. Subsequent to initial measurement, debt instruments are measured at amortised cost using the effective interest method.

Commodity contracts – Where possible, the Group takes the own use exemption permitted by IAS 39 for commodity contracts entered into and held for the purpose of the Group's own purchase, sale or usage requirements. Commodity contracts which do not qualify for the own use exemption are dealt with as derivatives and are recorded at fair value on the balance sheet with changes in fair value reflected through the income statement, or the hedge reserve to the extent that contracts are considered to be effective hedges.

Treasury derivatives – The Group uses a number of derivatives to manage exposure to interest rate and currency fluctuations. Treasury related derivatives are recorded at fair value on the balance sheet with changes in fair value reflected through the income statement, or the hedge reserve to the extent that derivatives are considered to be effective hedges. Income statement movements under interest rate hedges are accounted for as adjustments to finance cost / income for the period.

Share capital – Ordinary shares are classified as equity. 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 the difference between the nominal value of shares issued and the fair value of the consideration received.

Cash at bank and in hand – Cash at bank and in hand 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. For the purposes of the cash flow statement, cash and cash equivalents excludes debt service reserve and escrow account balances as these balances are restricted and can only be used for the purposes of debt service, and payment of certain Refinancing and Listing fees and expenses respectively.

Trade receivables – Trade receivables are recognised initially at fair value less provision for impairment. 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 receivables.

4. Financial Risk Management

The Group's activities expose it to a variety of financial risks including commodity price risk, counterparty risk, interest rate risk and foreign currency 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 a Trading and Risk Management Committee and central treasury function which identify, evaluate and hedge financial risks in close co-operation with the Group's trading function under policies approved by the Board of directors.

COMMODITY RISK

The Group is exposed to the effect of fluctuations in commodity prices, particularly the price of electricity, which is the commodity produced by the Group, as well as the price of coal (and other fuels), which is essential to the production of electricity, and since 1 January 2005, the price of carbon 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 making sales of power when profitable compared with marginal costs of fuel and carbon emissions allowances.

The Group purchases coal on either fixed or variable priced contracts with different maturities from a variety of domestic and international sources. The Group purchases carbon emissions allowances on fixed price contracts with different maturity dates from a range of domestic and international sources.

COUNTERPARTY RISK

As the Group relies on third-party suppliers for the delivery of coal and other goods and services, it is exposed to the risk of non-performance by these third-party suppliers.

The Group purchases a significant majority of its coal under contracts with UK Coal Mining Limited ("UK Coal"). There is a risk that if UK Coal falls into financial difficulty and / or fails to deliver against the contracts, there would be additional costs associated with securing coal from other suppliers. Should UK Coal fall into administration, the Group could be subject to temporary loss of deliveries, higher coal prices and accelerated payments.

The Group enters into fixed price 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.

The investment of surplus cash is undertaken to maximise the return within Board approved policies. These policies set out minimum rating requirements, maximum investment with any one counterparty and the maturity profile.

INTEREST RATE RISK

The Group is exposed to interest rate risk principally in relation to its outstanding bank debt. In particular, it is exposed to changes in the LIBOR interest rate of sterling-denominated debt, as substantially all of its debt is both: i) denominated in sterling; and ii) and has a variable LIBOR rate. The Group partially manages this risk with interest rate hedges on a proportion of its debt facilities. Information about the Group's instruments that are exposed to interest rate risk and their repayment schedules is included in note 16.

FOREIGN CURRENCY RISK

Foreign currency exchange contracts are principally entered into to hedge the Group's requirement to purchase coal from international sources in US dollars and to purchase carbon emissions allowances in Euros.

5. Other Exceptional Operating Income and Expenses

	Years ended 31 December	
	2005	2004
	£'m	£'m
Other exceptional operating income:		
Income from TXU administration	310.9	-
Reversal of impairment of tangible fixed assets (note 10)	19.0	-
Total other exceptional operating income	329.9	-
Other exceptional operating expenses:		
LTIP expenses arising on cash and share-based transactions (note 21)	(37.6)	-
Refinancing and Listing fees and expenses	(29.0)	-
Total other exceptional operating expenses	(66.6)	-

INCOME FROM TXU ADMINISTRATION

On 14 October 2002, TXU Corporation withdrew financial support for its subsidiary TXU Europe Group Plc ("TXU Group"). As a consequence of this, on 18 November 2002, Drax Power Limited terminated the TXU Hedging Contract with TXU Europe Energy Trading Limited ("TXU Europe"), a subsidiary of TXU Group, to minimise financial exposure due to credit risk. On terminating the TXU Hedging Contract, Drax Power Limited issued a claim (the "TXU Claim"), ultimately agreed by the Administrators of TXU Europe and TXU Group at approximately £348 million (including VAT), in respect of unpaid power purchased by TXU Europe and liquidated damages for default under the TXU Hedging Contract. The claim was not recognised in the financial statements in 2002.

On 30 March 2005, the Group received a first distribution of £204.7 million (net of VAT and a payment by the Group to TXU Europe Limited) under the TXU Claim. This amount was subsequently paid to B Debt holders on 15 April 2005 (note 16). On 2 August 2005, the Group received a second distribution of £51.1 million (net of VAT) under the TXU Claim. This amount was subsequently paid to B Debt holders on 17 August 2005 (note 16). On 19 January 2006,

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the Group received a third distribution of £55.1 million (net of VAT) under the TXU Claim. The third distribution has been recognised in the year ended 31 December 2005 and, together with the first and second distributions, resulted in total exceptional operating income of £310.9 million for the year. The third distribution is included as a receivable balance at 31 December 2005 (note 13). This amount was used to make a prepayment of the Group's Bridge loan on 23 January 2006 (note 16).

At the time of approving the financial statements the Group had a further £26 million (including VAT) outstanding under the TXU Claim. The directors have reasonable expectations that the Group will receive repayment of this amount broadly in full by early in 2007. However, due to the contingent nature of insolvency proceedings, there remains uncertainty over the timing and amount of further distributions to be determined by the TXU Administrators, and consequently these further amounts have not been recognised in the financial statements at 31 December 2005.

REFINANCING AND LISTING FEES AND EXPENSES

The total costs of the Refinancing and Listing, including costs and expenses of or incidental to preparation of the Prospectus, Admission costs, registration fees and costs of printing and distribution as well as fees and expenses related to the Group's new debt facilities amounted to £44.7 million. £29.0 million (£20.3 million net of tax) of these costs have been included within other exceptional operating expenses in the income statement. The remaining £15.7 million has been deducted from debt and is being amortised to interest payable over the duration of the Group's new debt facilities (note 16).

Of the total Refinancing and Listing fees and expenses, £7.4 million had not been paid as at 31 December 2005 and was included within trade and other payables (note 15).

6. Operating Profit

	Years ended 31 December	
	2005 £'m	2004 £'m
The following charges have been included in arriving at operating profit:		
Staff costs (note 29)	29.1	26.4
Depreciation of property, plant and equipment (all owned assets)	31.0	33.0
Loss on the disposal of property, plant and equipment	0.2	2.0
Provision for impairment of inventory	–	0.7
Repairs and maintenance expenditure on property, plant and equipment	32.0	34.9
Other operating expenses	88.6	89.9
Total other operating expenses excluding exceptional items and unrealised losses on derivative contracts	180.9	186.9

AUDITORS' REMUNERATION

During the year the Group obtained the following services from its auditors, Deloitte & Touche LLP, at costs as detailed below:

	Years ended 31 December	
	2005 £'000	2004 £'000
Audit services	310	227
Other services	415	90
	725	317

The increase in fees for other services in 2005 related to services provided in relation to both the adoption of IFRS and the Refinancing and Listing.

7. Finance Costs

	Years ended 31 December	
	2005 £'m	2004 £'m
Interest payable and similar charges:		
Interest payable on bank borrowings	(91.1)	(101.2)
Amounts payable on termination of interest rate swaps	(23.1)	–
Amortisation of deferred financing costs	(0.2)	–
Total interest payable and similar charges	(114.4)	(101.2)
Interest receivable:		
Interest income	5.8	4.6
Credit in respect of previously recognised unrealised losses on interest rate swaps terminated during the year (note 18)	17.7	–
Total interest receivable	23.5	4.6

8. Taxation

	Years ended 31 December	
	2005 £'m	2004 £'m
Tax credit comprises:		
Current tax	(5.5)	2.3
Deferred tax	24.3	32.8
	18.8	35.1
	Years ended 31 December	
	2005 £'m	2004 £'m
Tax on items charged to equity:		
Deferred tax on actuarial losses on defined benefit pension schemes	2.5	1.8
Deferred tax recognised on adoption of IAS 32 and IAS 39	1.7	-
Deferred tax recognised on fair value losses on cash flow hedges	32.9	-
	37.1	1.8

The tax differs from the standard rate of corporation tax in the UK (30% for both years). The differences are explained below:

	Years ended 31 December	
	2005 £'m	2004 £'m
Profit / (loss) before tax	263.6	(41.6)
Profit / (loss) before tax multiplied by rate of corporation tax in the UK (30% for both years)	79.1	(12.5)
Effects of:		
Adjustments in respect of prior periods	(6.2)	(2.3)
LTIIP tax deduction	(9.4)	-
Expenses not deductible for tax purposes	2.9	-
Tax effect of funding arrangements	(0.8)	(21.6)
Other	(0.1)	1.3
Tax losses utilised	(84.3)	-
Total taxation (continuing operations)	(18.8)	(35.1)

Under the current financing structure, Drax Holdings Limited ("Holdings"), a wholly owned subsidiary undertaking of the Company, is partially funded by a Eurobond payable to another group company, with a tax deduction being claimed for all of the corresponding interest charged in the Holdings income statement. Were HM Revenue & Customs to successfully challenge the deductions claimed in respect of the Eurobond coupons for open years to 31 December 2005, it is estimated that the additional tax liability would be up to £70 million, together with interest and penalties.

9. Earnings per Share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year. The calculation of weighted average number of ordinary shares outstanding assumes that the ordinary shares in Drax Group plc issued to the existing shareholders of Drax Group Limited on Refinancing and Listing were in issue either at 1 January 2004 (to the extent that the related Drax Group Limited shares were in issue at 1 January 2004), or from the date of issue of Drax Group Limited shares (to the extent that the related Drax Group Limited shares were issued after 1 January 2004).

The Group has no contingently issuable shares. Accordingly, there is no difference between basic and diluted earnings per share.

Reconciliations of the earnings and weighted average number of shares used in the calculation are set out below.

	Years ended 31 December	
	2005	2004
Earnings attributable to equity holders of the Company (£'m)	282.4	(6.5)
Weighted average number of shares (millions)	288.2	275.2
Basic and diluted earnings per share (pence per share)	98.0	(2.4)

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10. Impairment Tests for Goodwill and Fixed Assets

During the year to 31 December 2002, the Group performed an impairment review following the loss of the TXU Hedging Contract and its related income streams. This resulted in the write down of goodwill to nil, and a provision for impairment of £20.4 million against tangible fixed assets, to write down the assets to their estimated recoverable amount.

In accordance with IAS 36, the Group assessed at each subsequent reporting date whether there was any indication that the impairment loss recognised at 31 December 2002 should be reversed. As a result of the assessment performed at 30 June 2005 for the purposes of the financial information prepared in connection with the Refinancing and Listing, which highlighted significant increases in wholesale electricity prices that the Group has been able to achieve in its forward contractual position, the Group recorded a reversal of the tangible fixed asset impairment of £19.0 million (£13.3 million net of tax). This represents a reversal of the total impairment loss recognised in respect of tangible fixed assets at 31 December 2002 after adjusting for depreciation (note 5).

The assessments are performed using value-in-use calculations based on a long-term discounted cash flow model designed specifically for the purposes of the impairment review. The key assumptions used in the model include: power generation levels, power prices, fuel prices, operating cost inflation, capital expenditure and the discount rate.

An indication of the key assumptions used for the value-in-use calculations performed at 31 December 2004 and 30 June 2005 is set out below:

	As at 31 December 2004	As at 30 June 2005
Average annual amounts included in long-term discounted cash flow model for:		
Generation (million MWh)	21.6	21.0
Power price (£/MWh)	44.7	45.8
Gross margin (%)	57.5	60.4
Operating cost inflation (%)	1.9	2.3
Capital expenditure (£'m)	15.2	22.5
Discount rate (%)	12.2	12.3

Power and fuel prices were based on forward curves for the periods for which they were available and generation on plant availability and forecast generation profiles at the time of performing the reviews. Projected power and fuel prices were calculated utilising growth rates between 2.5% and 2.7% beyond available forward curves. The discount rate applied was the pre-tax rate based upon the Group's weighted average cost of capital at the time of performing the reviews (i.e. prior to the Refinancing and Listing on 15 December 2005).

The directors consider with reference to both external and internal sources of information that no indication of impairment existed as at 31 December 2005. Accordingly a value-in-use calculation has not been performed at 31 December 2005 for the purposes of IAS 36.

11. Property, Plant and Equipment

	Land and buildings £'m	Plant and equipment £'m	Plant spare parts £'m	Total £'m
Cost:				
At 1 January 2004	132.2	1,090.1	24.0	1,246.3
Additions at cost	0.5	11.4	1.8	13.7
Disposals	-	(2.5)	-	(2.5)
Issues	-	-	(0.6)	(0.6)
At 1 January 2005	132.7	1,099.0	25.2	1,256.9
Additions at cost	0.9	20.8	5.3	27.0
Disposals	-	(4.0)	-	(4.0)
Issues	-	-	(2.0)	(2.0)
At 31 December 2005	133.6	1,115.8	28.5	1,277.9
Accumulated depreciation:				
At 1 January 2004	16.1	168.8	2.1	187.0
Charge for the year	3.2	29.2	0.6	33.0
Disposals	-	(0.8)	-	(0.8)
At 1 January 2005	19.3	197.2	2.7	219.2
Charge for the year	3.2	27.2	0.6	31.0
Disposals	-	(3.8)	-	(3.8)
Reversal of impairment	-	(19.0)	-	(19.0)
At 31 December 2005	22.5	201.6	3.3	227.4
Net book amount at 31 December 2004	113.4	901.8	22.5	1,037.7
Net book amount at 31 December 2005	111.1	914.2	25.2	1,050.5

Details of impairment reviews performed are included in note 10 above.

12. Inventories

	As at 31 December	
	2005 £'m	2004 £'m
Raw materials and consumables	56.7	41.4
Renewables Obligation Certificates	11.1	3.8
	67.8	45.2

The Group's inventory consumption was £309.9 million in 2004 and £372.2 million in 2005.

13. Trade and Other Receivables

	As at 31 December	
	2005 £'m	2004 £'m
Amounts falling due within one year:		
Trade debtors	128.4	63.5
Prepayments and other debtors	64.5	6.0
	192.9	69.5

Included within prepayments and other debtors as at 31 December 2005 is £56.8 million (including VAT) that was received on 19 January 2006 in respect of the TXU Claim (note 5).

Trade debtors generally represent sales of electricity to a number of counterparties. At 31 December 2005, the Group had amounts receivable from 6 (2004: 5) significant counterparties, and a number of smaller counterparties, all of which generally pay within 15 days of receipt of invoice. Management do not consider there to be a significant concentration of credit risk and as a result, do not believe that a further credit risk provision is required in excess of the normal provision for doubtful debts.

Notes to the Consolidated Financial Statements continued

14. Cash at Bank and In Hand

	As at 31 December	
	2005 £'m	2004 £'m
Cash at bank and in hand:		
Unrestricted cash at bank and in hand	87.8	37.5
Debt service reserve account	-	38.2
Escrow account	11.3	-
	99.1	75.7

Debt service reserve account balances were restricted cash deposits which could only be used for the purpose of debt service under the terms of the Group's previous debt facilities.

The escrow account represents cash paid into escrow prior to 15 December 2005 with respect to certain fees and expenses related to the Refinancing and Listing. The directors expect substantially all such fees and expenses will have been paid out of the escrow account by 31 March 2006.

Cash and cash equivalents includes the following for the purposes of the cash flow statement:

	As at 31 December	
	2005 £'m	2004 £'m
Cash and cash equivalents:		
Cash at bank and in hand per above	99.1	75.7
Less: debt service reserve and escrow accounts	(11.3)	(38.2)
	87.8	37.5

15. Trade and Other Payables

	As at 31 December	
	2005 £'m	2004 £'m
Amounts falling due within one year:		
Trade payables	20.7	6.2
Other creditors	16.5	14.1
Accruals	106.6	46.1
Other tax and social security payable	32.3	0.5
	176.1	66.9

Accruals at 31 December 2005 include an amount of £50.4 million with respect to the Group's estimated net liability to deliver carbon emissions allowances. The amount provided represents an estimate of the amounts that will be required to satisfy the net obligation related to generation at the balance sheet date, taking into account free allowances allocated under the National Allocation Plan, market purchases and forward contracts already in place.

16. Financial Liabilities – Borrowings

	As at 31 December	
	2005 £'m	2004 £'m
Current:		
Term loan	46.3	-
Bridge loan	55.1	-
B Debt	-	204.7
	101.4	204.7
Non-current:		
Term loan	438.2	-
Bridge loan	21.9	-
A Debt	-	944.9
B Debt	-	133.7
	460.1	1,078.6

MATURITY OF BORROWINGS

The maturity profile of the carrying amount of the Group's non-current borrowings at the balance sheet dates were as follows:

	As at 31 December	
	2005 £'m	2004 £'m
Non-current:		
In more than one year but not more than two years	31.6	130.0
In more than two years but not more than five years	428.5	85.0
In more than five years	-	863.6
	460.1	1,078.6

The effective interest rates at the balance sheet dates were as follows:

	31 December 2005 %	31 December 2004 %
Term loan	5.55	-
Bridge loan	5.55	-
A1 Debt	-	7.43
A2 Debt	-	8.93
A3 Debt	-	9.93
B Debt	-	6.93

BORROWINGS AT 31 DECEMBER 2004

The Group's debt structure consisted of loans and notes held by InPower 2 Limited ("InPower 2") and NoteCo Limited ("NoteCo"). InPower 2 and NoteCo are special purpose entities resident in Jersey and were utilised specifically for the purpose of holding the debt of the Group. Although InPower 2 and NoteCo are not subsidiary undertakings of Drax Group Limited, in accordance with SIC 12 "Consolidation – Special Purpose Entities", they have been fully consolidated within these financial statements on the basis that their sole purpose was to hold the debt of the Group prior to the Refinancing and Listing on 15 December 2005.

The Group's borrowings consisted of four tranches of floating rate debt as follows:

	As at 31 December 2004		
	Loans £'m	Notes £'m	Total £'m
A1 Debt	279.4	120.5	399.9
A2 Debt	321.3	137.4	458.7
A3 Debt	60.6	25.8	86.4
B Debt	237.3	101.0	338.3
Total borrowings	898.6	384.7	1,283.3
Less current portion of B Debt	(143.6)	(61.1)	(204.7)
Non-current borrowings	755.0	323.6	1,078.6

The A1 Debt was the first ranking tranche of the secured debt. The A1 Debt was subject to a fixed amortisation profile beginning on 30 June 2007 and ending on 30 June 2015. The A1 Notes were listed on the Luxembourg Stock Exchange on 29 June 2004. Following a prepayment of £11.7 million on 30 June 2005, £388.2 million of A1 Debt principal and £12.8 million of interest was outstanding prior to the Refinancing and Listing.

The A2 and A3 Debt were second and third ranking tranches of the secured debt respectively. The A2 and A3 Debt had no fixed amortisation profile, the outstanding principal balances falling due for payment on 30 June 2015 and 30 June 2020 respectively. Both the A2 and A3 Notes were listed on the Channel Islands Stock Exchange on 29 June 2004. Prior to the Refinancing and Listing, £545.1 million of A2/A3 Debt principal and £22.2 million of interest was outstanding.

The B Debt was the fourth ranking tranche of the secured debt, but had a first priority over the TXU Claim and the proceeds thereof, which were its primary source of repayment. The B Debt had no fixed amortisation profile with the outstanding principal balance falling due for payment on 30 June 2025. The B Notes were listed on the Luxembourg Stock Exchange on 27 June 2005. Following partial repayments of £204.7 million on 15 April 2005 after the first distribution under the TXU Claim and £51.1 million on 17 August 2005 after the second distribution, £82.4 million B Debt principal and £28.1 million of interest was outstanding prior to the Refinancing and Listing.

Notes to the Consolidated Financial Statements continued

REFINANCING AND LISTING

Pursuant to the schemes of arrangement under which the Refinancing and Listing was implemented, the Group's debt was restructured on 15 December 2005. The particular elements of the restructuring relating to the Group's debt are illustrated below:

	As at 15 December 2005	
	Principal £'m	Interest £'m
Previous debt facilities:		
A1 Debt prepayment	388.2	12.8
B Debt prepayment	82.4	28.1
A2 Debt cash consideration	112.0	-
A2/A3 Debt interest payment	-	22.2
Interest rate swap termination payment	-	23.1
	582.6	86.2
New debt facilities:		
Term loan	500.0	-
Bridge loan	77.0	-
	577.0	-

Outstanding principal and interest in relation to A1 and B Debt was repaid in full. In addition, interest rate swap contracts with a notional value of £400 million, principally related to A1 Debt, were terminated.

A2/A3 Debt holders contributed their A2/A3 Debt in exchange for cash and ordinary shares of 10 pence each in Drax Group plc. A2 Debt holders received 21,668 ordinary shares and £24,421 for each £100,000 of A2 Debt. A3 Debt holders received 28,669 ordinary shares for each £100,000 of A3 Debt. In total A2 Debt holders received cash consideration of £112.0 million and A2/A3 Debt holders received 124,164,221 ordinary shares of 10 pence each in Drax Group plc. Outstanding interest on A2/A3 Debt was repaid in full.

The Group settled the remaining nominal value of A2/A3 Debt, after deduction of the A2 cash consideration, of £433.1 million in exchange for issuing the 124,164,221 ordinary shares in Drax Group plc. The directors determined that the nominal value of A2/A3 Debt approximated its fair value by reference to the terms of the debt, principally the ability to prepay at nominal value (note 18). The nominal value of shares issued of £12.4 million was therefore lower than the fair value of the asset acquired of £433.1 million. Under section 130 of the Companies Act 1985, the shares are treated as issued fully paid up and the difference of £420.7 million is recorded as share premium (note 27).

The total cash outflows related to the Refinancing and Listing were partially funded by a new Term loan of £500.0 million and a Bridge loan of £77.0 million as described below. The remaining cash outflows, including the payment of fees and expenses (note 5), were principally funded by cash generated from operations.

BORROWINGS AT 31 DECEMBER 2005

Borrowings at 31 December 2005 consisted of bank loans held by the Company's subsidiary undertaking Drax Finance Limited as follows:

	As at 31 December 2005		
	Borrowings before deferred finance costs £'m	Deferred finance costs (note 5) £'m	Net borrowings £'m
Term loan	500.0	(15.5)	484.5
Bridge loan	77.0	-	77.0
Total borrowings	577.0	(15.5)	561.5
Less current portion of debt	(105.1)	3.7	(101.4)
Non-current borrowings	471.9	(11.8)	460.1

The Term loan is subject to a fixed amortisation profile beginning on 30 June 2006 and ending on 31 December 2010.

The Bridge loan has a first priority over the TXU Claim and the proceeds thereof, which are its primary source of repayment. Following a third distribution under the TXU Claim on 19 January 2006, £55.1 million of the Bridge loan was repaid on 23 January 2006. The third distribution has been recognised in the year ended 31 December 2005 and has been included as a receivable balance at 31 December 2005 (note 13). The debt which was repaid on 23 January 2006 has been shown as repayable within one year at 31 December 2005. The Bridge loan has no fixed amortisation profile. Any outstanding principal balance falls due for payment on 31 December 2008.

Ultimately, the Group's ability to make repayments of the Term loan is entirely dependent on the successful operation of the business. The ability of the Group to make repayment of the Bridge loan is dependent on: i) the timing and quantum of recoveries under the TXU Claim; and ii) to the extent that such recoveries are insufficient to pay amounts under the Bridge loan when due, the successful operation of the business.

The Group's debt is guaranteed and secured by each of the principal subsidiary undertakings of the Company, as stated in note 3 to the Company's separate financial statements, and also by the Company.

Payment profiles for repayment of debt set out above are based on the fixed minimum repayment profile. Repayments above the fixed minimum repayment profile are permitted subject to the amount of cash available for debt service. With the exception of Bridge loan principal repayments, debt service payments are made semi-annually on 30 June and 31 December. The timing of Bridge loan repayments is determined by receipts under the TXU Claim.

LETTER OF CREDIT FACILITY AND REVOLVING CREDIT FACILITY

In addition to its borrowings, the Group has access to a letter of credit facility which provides credit support of up to £200 million to the Group's trading activities. The letter of credit facility, which has a final maturity date of 15 December 2012, provides a mechanism whereby it may be extended at any time after 15 December 2007, but no later than one year before the final maturity date. The Group guarantees the obligations of a number of banks in respect of the letters of credit issued by those banks to counterparties of the Group. As at 31 December 2005 the Group's contingent liability in respect of these guarantees amounted to £77.4 million (2004: £26.5 million).

In addition, the Group has access to an undrawn £100 million revolving credit facility, which may be used to issue letters of credit or for working capital, with a final maturity date of 15 December 2010.

17. Other Non-current Liabilities

	As at 31 December	
	2005 £'m	2004 £'m
Interest accrual	-	25.0
Retentions	0.7	0.8
	0.7	25.8

The interest accrual includes £nil (2004: £25.0 million) deferred interest with respect to the Group's B Debt. This interest was paid in full on Refinancing and Listing, and was treated as falling due in more than five years under the terms of the Group's previous debt facilities. The retention liabilities relate to amounts held back from certain suppliers pending satisfaction of contractually agreed performance criteria. The Group estimates that substantially all retention liabilities will fall due for payment in more than one year but in not more than two years.

18. Derivatives and Financial Instruments

The Group issues or holds financial instruments for two purposes:

- Financial instruments relating to the operations, financing and risks of the Group's operations.
- Financial instruments relating to the financing and risks of the Group's debt portfolio.

The Group's financial instruments comprise borrowings, cash and liquid resources, items that arise directly from its operations and derivative transactions. The Group also enters into short and medium term forward sales contracts for the sale of electricity and the purchase of coal and carbon emissions allowances.

As permitted under IFRS 1, the Group has taken advantage of the exemption not to restate comparative information for IAS 39. As a result, IAS 32 and IAS 39 are applicable for the Group from 1 January 2005. For the period prior to the adoption of IAS 39, the Group has applied UK GAAP accounting rules for derivatives and financial instruments. The numerical disclosures immediately below illustrate the financial assets and liabilities as defined in IAS 32 relating to the year ended 31 December 2005. The subsequent FRS 13 "Derivatives and Other Financial Instruments: Disclosures" set out numerical disclosures relating to the year ended 31 December 2004. Certain financial assets and liabilities, such as investments in subsidiary companies are excluded from the scope of these disclosures. As permitted by FRS 13, short-term debtors and creditors have also been excluded from the disclosures.

IAS 32 "FINANCIAL INSTRUMENTS: DISCLOSURE AND PRESENTATION": YEAR ENDED 31 DECEMBER 2005

From 1 January 2005, as noted above, the Group has adopted both IAS 32 and IAS 39. Were IAS 32 and IAS 39 to have been applied during the year to 31 December 2004 the impact would have been to reduce net assets at 31 December 2004 by £3.9 million (net of tax) and to record a credit in the income statement of £26.7 million (net of tax) for the year ended 31 December 2004.

The Group recognised a reduction in net assets and retained earnings of £5.6 million (£3.9 million net of tax) at 1 January 2005, being an adjustment to reflect the fair value of derivative financial instruments in the balance sheet at that time.

Notes to the Consolidated Financial Statements continued

The following table sets out the fair value of financial instruments at 1 January 2005, the date of adoption of IAS 32 and IAS 39, and as at 31 December 2005:

	1 January 2005		31 December 2005	
	Assets £'m	Liabilities £'m	Assets £'m	Liabilities £'m
Commodity contracts	14.5	2.5	7.2	222.4
Interest rate swaps	–	17.7	–	–
Forward foreign currency exchange contracts	0.1	–	0.8	0.2
Total	14.6	20.2	8.0	222.6
Less: non-current portion				
Commodity contracts	–	(1.2)	(0.3)	(49.6)
Current portion	14.6	19.0	7.7	173.0

COMMODITY CONTRACTS

The Group enters into short and medium term forward electricity sales contracts to hedge generation output. The Group also purchases coal and carbon emissions allowances under contracts from a range of domestic and international suppliers. Due to the nature of some of these contracts and the way they are managed, the own use exemption within IAS 39 has only been applied to a limited number of them. For the purposes of IAS 39, from 1 July 2005, the Group has put in place appropriate hedge accounting documentation to enable it to achieve hedge accounting for a large proportion of its commodity contracts. As a result, mark-to-market movements on contracts which are now considered to be effective hedges are recognised through the hedge reserve. For the period from 1 January 2005 to 30 June 2005, mark-to-market movements on these contracts were reflected directly in the income statement, as appropriate hedge documentation had not been put in place.

The fair value of commodity contracts qualifying as derivative financial instruments is calculated by reference to forward market prices which are available 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.

INTEREST RATE SWAPS

The Group enters into interest rate swap arrangements to hedge variable interest costs on the Group's debt. At 31 December 2004, the notional principal amounts of outstanding interest rate swap contracts was £400 million. As described in note 16, the Group terminated these interest rate swap contracts on Refinancing and Listing on 15 December 2005, resulting in a credit adjustment to release the previously recognised unrealised losses of £17.7 million and a termination payment of £23.1 million, both of which have been included in finance costs for the year (note 7). As required under the terms of the Group's new debt facility agreements effective 15 December 2005, interest rate swap contracts with notional principal amounts of £250 million were entered into on 5 January 2006. Accordingly, no interest rate swap contracts were outstanding at the year-end.

FORWARD FOREIGN CURRENCY EXCHANGE CONTRACTS

Foreign currency exchange contracts are principally entered into to hedge the Group's requirement to purchase coal from international sources in US dollars, and to purchase carbon emissions allowances in Euros. The fair value of forward foreign currency exchange contracts is determined using forward exchange market rates at the balance sheet date.

EMBEDDED DERIVATIVES

The Group has also reviewed all 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 to be separately valued from their host contracts.

The amounts recorded in the income statement in respect of derivatives which are marked to market are as follows:

	For the year ended 31 December 2005 £'m
Unrealised loss on derivative contracts recognised in arriving at operating profit	(117.0)
Credited to interest receivable in respect of derivative contracts terminated during the year	17.7
	(99.3)

The amounts recorded in the hedge reserve in respect of derivatives which are marked to market are as follows:

	For the year ended 31 December 2005 £m
Unrealised loss on hedging derivative contracts	(109.7)

NET FAIR VALUES OF DERIVATIVE FINANCIAL INSTRUMENTS

The net fair values of derivative financial instruments were:

	As at 31 December 2005 £m
Contracts with positive fair values	
Forward foreign currency exchange contracts	0.6
Contracts with negative fair values	
Commodity contracts	(215.2)

The carrying amounts of cash at bank and in hand, trade and other receivables, and trade and other payables approximate their fair value. As a result of their terms, the carrying amounts of the Term and Bridge loans approximate their fair value.

FRS 13 "DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS: DISCLOSURES": YEAR ENDED 31 DECEMBER 2004

FINANCIAL ASSETS

The Group's financial assets comprise deposits made with banks and which earn interest at various rates. At 31 December 2004 all of the Group's financial assets, which totalled £75.7 million, were denominated in sterling and were subject to floating interest rates.

FINANCIAL LIABILITIES

At 31 December 2004 the Group's financial liabilities comprised A Debt of £945.0 million and B Debt of £338.3 million, that bore interest at rates based upon LIBOR for terms of up to six months.

After taking account of the various interest rate swaps entered into by the Group, the interest rate risk profile of the Group's gross financial liabilities was as follows:

Currency	Year ended 31 December 2004		
	Total £m	Floating rate financial liabilities £m	Fixed rate financial liabilities £m
Sterling	1,283.3	883.3	400.0

Currency	Year ended 31 December 2004		
	Weighted average interest rate %	Fixed rate financial liabilities – weighted average period for which rate is fixed Years	Weighted average period until maturity Years
Sterling	8.05	7.6	13.5

FAIR VALUE DISCLOSURES

Set out below is a comparison of book values and fair values of the Group's financial assets and liabilities. Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed willing parties and excludes accrued interest. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated by discounting expected cash flows at prevailing interest rates and applying year end exchange rates.

Notes to the Consolidated Financial Statements continued

	31 December 2004	
	Book value £m	Fair value £m
Financial assets		
Bank deposits	75.7	75.7
Primary financial instruments issued to finance the Group's operations		
Net borrowings	1,283.3	1,283.3
Derivative financial instruments held to manage the interest rate profile		
Interest rate swaps	–	(17.7)

The carrying amounts of the financial assets approximate their fair value. The carrying amount of the A Debt and B Debt approximated their fair value as a result of their terms, principally the ability of the Group to prepay the debt at nominal value.

The fair value of the interest swaps have been determined by reference to prices available from the markets on which these instruments or similar instruments are traded.

GAINS AND LOSSES ON FINANCIAL ASSETS AND FINANCIAL LIABILITIES HELD OR ISSUED FOR TRADING

No gains or losses have been recognised which relate to trading in financial assets and financial liabilities as the Group does not hold financial assets or financial liabilities for trading purposes.

GAINS AND LOSSES ON FORWARD CONTRACTS

The Group uses interest rate swaps to manage its interest rate exposure. Changes in the fair value of instruments used as hedges are not recognised in the financial statements until the hedged position matured. An analysis of unrecognised gains and losses is as follows:

	Year ended 31 December 2004		
	Gains £m	Losses £m	Net £m
Unrecognised gains and losses on forward contracts at 1 January	–	(12.9)	(12.9)
Gains and losses arising in previous years that were recognised in the year	–	–	–
Gains and losses arising before 1 January that were not recognised in the year	–	(12.9)	(12.9)
Gains and losses arising in the period that were not recognised in the year	–	(4.8)	(4.8)
Unrecognised gains and losses at 31 December	–	(17.7)	(17.7)
Gains and losses expected to be recognised in the next financial year	–	–	–
Gains and losses expected to be recognised after the next financial year	–	(17.7)	(17.7)

19. Provisions

	Re-instatement	LTIP	Total
	£m	£m	£m
At 1 January 2004	0.1	–	0.1
Additional provision in the year	–	0.4	0.4
At 31 December 2004	0.1	0.4	0.5
Additional provision in the year	1.9	4.7	6.6
Utilisation of provision	–	(5.1)	(5.1)
At 31 December 2005	2.0	–	2.0

RE-INSTATEMENT

Provision for re-instatement represents the estimated decommissioning, demolition and site remediation costs at the end of the useful economic life of the Group's generating assets, on a discounted basis. The amount provided represents the present value of the expected costs. An amount equivalent to the initial provision is capitalised within tangible fixed assets and is depreciated over the useful lives of the related assets. The unwinding of the discount is included in interest payable and similar charges.

The provision is estimated using the assumption that the re-instatement will take place between 2039 and 2045. The provision has been estimated using existing technology at current prices. The discount rate applied is the pre-tax rate based upon the Group's weighted average cost of capital and reflects the current market assessment of the time value of money and the risks specific to the business.

LONG-TERM INCENTIVE PLAN ("LTIP")

Provision for the LTIP (note 21) represents costs associated with the cash-based award component of the scheme. The maximum total cash payment over the life of the plan was £5.1 million, with the timing of payments being linked to repayment of the Group's eligible debt, and the cost originally recognised in the income statement on a straight line basis over the expected debt repayment period on an undiscounted basis.

As a result of the Refinancing and Listing on 15 December 2005 and the resulting repayment of the eligible debt, the full £5.1 million cash-based award payable under the LTIP vested. Under the terms of the LTIP, 50% of payments to be made to directors, business and team leaders, totalling £1.7 million, have been deferred until the first anniversary of the Refinancing and Listing. This amount is included within trade and other payables (note 15).

20. Deferred Tax

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 30% (2004: 30%). The movement on the deferred tax account is as shown below:

	As at 31 December	
	2005 £'m	2004 £'m
Deferred tax liability at the beginning of the year	246.7	281.3
Credited to income statement	(24.3)	(32.8)
Deferred tax on actuarial losses on defined benefit pension schemes	(2.5)	(1.8)
Deferred tax recognised on adoption of IAS 32 and IAS 39	(1.7)	--
Deferred tax recognised on fair value losses on cash flow hedges	(32.9)	--
Deferred tax liability at the end of the year	185.3	246.7

The movements in deferred tax assets and liabilities during the period are shown below. Deferred tax assets and liabilities are offset where there is a legally enforceable right of offset and there is an intention to settle the balances net.

	Accelerated capital allowances	Other	Total	
	£'m	£'m	£'m	
Deferred tax liabilities:				
At 1 January 2004	290.0	--	290.0	
Credited to income statement	(4.1)	--	(4.1)	
At 31 December 2004	285.9	--	285.9	
Charged to income statement	0.6	10.1	10.7	
At 31 December 2005	286.5	10.1	296.6	
	Financial Instruments	Tax losses	Other	Total
	£'m	£'m	£'m	£'m
Deferred tax assets:				
At 1 January 2004	--	--	8.7	8.7
Credited to income statement	--	28.7	--	28.7
Credited to equity	--	--	1.8	1.8
At 31 December 2004	--	28.7	10.5	39.2
Credited to income statement	29.8	0.6	4.6	35.0
Credited to income statement reserves following the introduction of IAS 39	1.7	--	--	1.7
Credited to equity	32.9	--	2.5	35.4
At 31 December 2005	64.4	29.3	17.6	111.3

Deferred tax assets are recognised in respect of tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. Tax loss carry-forwards have not been recognised where the realisation of the related tax benefit through future taxable profits is not assessed as probable. As at 31 December 2005 the unrecognised tax benefit amounted to £1.4 million (2004: £32.0 million).

21. Share-based Payments

LONG-TERM INCENTIVE PLAN ("LTIP")

At an extraordinary general meeting of the previous holding company, Drax Group Limited, held on 30 April 2004 shareholders approved:

- (1) the conversion of 7,782,480 un-issued ordinary shares in Drax Group Limited into non-voting shares;
- (2) the payment of £0.4 million to each of Gordon Horsfield and Gerald Wingrove (a director of Drax Group Limited at the time) in recognition of services rendered in connection with a restructuring of the debt of the Group approved on 22 December 2003 on the understanding that each of them would have the right (which each subsequently exercised) to purchase 1,729,440 of the non-voting shares referred to in paragraph (1); and
- (3) the establishment of a Long-Term Incentive Plan which would have at its disposal a cash pool of £5.1 million (the payment of which was dependant upon certain parts of the Group's debt being repaid) and 4,323,600 non-voting shares, being the total of the non-voting shares referred to in paragraph (1) less the number of shares purchased by Gordon Horsfield and Gerald Wingrove pursuant to the right referred to in paragraph (2).

The objective of the LTIP was to incentivise employees to create sustained value for the Group's debt holders and shareholders by repaying the Group's debt (including debt repayment through a shareholder approved refinancing at par) and increasing the value of the Group's equity. It provided for the making of:

- (a) Initial Awards, both of non-voting shares and cash units (giving a proportionate entitlement to sums from time to time payable out of the total of £5.1 million referred to in paragraph (3)), to employees selected by the Remuneration Committee and in post on 22 December 2003;

Notes to the Consolidated Financial Statements continued

- (b) Performance Share Awards of units which, subject to the satisfaction of any associated performance criteria and the other provisions of the LTIP rules, gave a proportionate entitlement to the non-voting shares held by the LTIP trustee (see below); and
- (c) Performance Cash Awards in the form of units which gave a proportionate entitlement to sums from time to time payable out of the total of £5.1 million referred to in paragraph (3).

Pursuant to Initial Share Awards, a total of 549,923 non-voting shares were purchased at a price of 13.65 pence per share by executive directors, business and team leaders. The remaining 3,773,677 non-voting shares (i.e. 7,782,480 non-voting shares referred to in paragraph (1) less the total number of shares purchased both as Initial Awards and by Gordon Horsfield and Gerald Wingrove pursuant to paragraph (2)) were subsequently issued to the LTIP trustee.

On 17 January 2005 and 13 June 2005, performance awards comprising both Performance Share Awards and Performance Cash Awards were made to executive directors, business and team leaders in recognition of their contribution to the Group's business. On 20 October 2005 performance awards comprising Performance Share Awards and Performance Cash Awards were made to all employees of the Group in post on 15 December 2005 (including executive directors, business and team leaders) in recognition of their contributions to the Group's business. These awards were conditional upon an Exit Event (see below) taking place prior to 31 January 2006.

The £5.1 million at the disposal of the LTIP represented 0.85% of the aggregate eligible debt at the time of establishment. Upon repayment of any part of the eligible debt, 0.85% of the amount repaid becomes payable to LTIP participants according to their respective entitlements determined by the cash units awarded to them.

Under the terms of the LTIP, upon the occurrence of certain types of transaction (an "Exit Event"), such as a sale of the Company or a listing of its equity on a recognised exchange, the holders of non-voting shares purchased by virtue of Initial Share Awards have the same rights (other than to vote) as the holders of ordinary shares, and all Performance Share Awards vest in the beneficiaries giving them a proportionate right, according to their respective holdings of units, to the non-voting shares held by the LTIP trustee (in relation to which they then have the same rights (other than to vote) as the holders of ordinary shares).

As a result of the Refinancing and Listing on 15 December 2005 (an Exit Event), all cash and share-based awards under the LTIP fully vested and exit rights occurred in both cases. Pursuant to the schemes of arrangement under which the Refinancing and Listing was implemented, existing shareholders in Drax Group Limited, including LTIP shareholders, received three ordinary shares of 10 pence each in Drax Group plc in exchange for each ordinary share in Drax Group Limited.

Directors, business and team leaders all agreed to be subject to certain voluntary sale restrictions in respect of the Drax Group plc shares they received under the LTIP. These voluntary restrictions provided that up to 50% of a participant's holding (i.e. shares subject to an Initial Share Award and the balance of the shares subject to a Performance Share Award once the associated tax liabilities have been discharged) can be sold at any time after the Refinancing and Listing. The balance of the participant's holding may be sold at any time after the first anniversary of the Refinancing and Listing.

Full repayment of eligible debt resulted in the total £5.1 million payable under the LTIP cash pool becoming due to participants. Under the terms of the LTIP, 50% of payments to be made to directors, business and team leaders, totalling £1.7 million, have been deferred until the first anniversary of the Refinancing and Listing. This amount is included within trade and other payables (note 15).

LTIP awards made up to 15 December 2005 are shown below.

Long-Term Incentive Plan – Awards	At 1 Jan 2004	Granted	At 31 Dec 2004	Exercise price	Vesting period from	Vesting period to
Total – Initial Units	–	250	250	–	28 May 2004	28 May 2004
Weighted average price of units	–	–	–			

Long-Term Incentive Plan – Awards	At 1 Jan 2004	Granted	At 31 Dec 2004	Exercise price	Vesting period from	Vesting period to
Initial units	250	–	250	–	28 May 2004	28 May 2004
Performance units	–	500 ⁽¹⁾	500 ⁽¹⁾	–	17 January 2006	13 June 2008
Total units	250	500 ⁽¹⁾	750 ⁽¹⁾	–		
Weighted average price of units	–	–	–			

(1) In addition to 500 Performance Share Award units, 750 Performance Cash Award units were granted in the year ended 31 December 2005, taking the total number of cash award units granted to 1,000 at 15 December 2005.

Costs recognised in the income statement in relation to the LTIP are as follows:

	Years ended 31 December	
	2005	2004
	£'m	£'m
LTIP expenses arising on share-based payment transactions	25.2	–
LTIP expenses arising on cash-based payment transactions	4.7	0.4
Social security costs arising on share and cash-based payment transactions	7.7	–
	37.6	0.4

The expense arising from share-based payment transactions for the year ended 31 December 2005 is determined from the Group's estimate of the market value of the shares included in the first Performance Share Award made on 17 January 2005. The valuation relates to all of the 3,773,677 shares held by the LTIP trustee, as under the terms of the LTIP, all such shares vest on the occurrence of an Exit Event. Although subsequent Performance Share Awards were made later in 2005, such awards served only to alter the proportionate rights of holdings in LTIP units of participants. The market value of these shares was estimated based on the market value on that date of the Group's A2 and A3 Debt, which was contractually linked to the ordinary voting shares. This amount has been charged to the income statement in full in 2005, following vesting of the awards on Refinancing and Listing on 15 December 2005. There is no expense arising from the shares purchased by Gordon Horsfield and Gerald Wingrove or from the Initial Share Awards, both in 2004, as the Group determined that the fair value of its equity was £nil at that time.

The remaining expense arising from cash-based payment transactions of £4.7 million (£0.4 million having been charged in 2004) has been charged to the income statement in full in 2005, following vesting of the awards on Refinancing and Listing on 15 December 2005.

Employer National Insurance contributions on cash and share-based payment transactions have also been included as an expense in 2005. The total charge with respect to the LTIP of £37.6 million (£26.3 million net of tax) has been included within exceptional other operating expenses in the income statement (note 5).

The Board believe that employee share ownership plays a significant role in the recruitment, motivation and retention of staff at all levels within the Group. The Group is therefore intending to establish certain new employee share plans to be administered by the Remuneration Committee.

22. Called-up Share Capital

	As at 31 December	
	2005 £'m	2004 £'m
Authorised		
2004 – 1,000,000,000 ordinary shares of 0.001p each	–	–
2005 – 999,500,020 ordinary shares of £0.10 each	100.0	–
Issued and fully paid		
2004 – 94,254,480 ordinary shares of 0.001p each	–	–
2005 – 406,927,661 ordinary shares of £0.10 each	40.7	–
	40.7	–

Under IFRS 3, the insertion of Drax Group plc as the new holding company has been accounted for as a reverse acquisition, whereby Drax Group Limited (being the previous holding company), the legal subsidiary, acquired Drax Group plc, the legal parent company. Therefore, the share capital in the consolidated balance sheet at 31 December 2004 reflected that of Drax Group Limited prior to the reverse acquisition.

DRAX GROUP LIMITED

There were 86,472,000 ordinary shares of 0.001 pence each of the previous holding company, Drax Group Limited issued as at 31 December 2003, which were contractually linked to the A2 and A3 Loans issued by InPower 2 and A2 and A3 notes issued by NoteCo (note 16).

At an extraordinary general meeting of Drax Group Limited on 30 April 2004 shareholders resolved to amend the authorised share capital of the Company by the conversion of 7,782,480 unissued ordinary shares in Drax Group Limited into 7,782,480 non-voting ordinary shares.

With the approval of shareholders given at the same Extraordinary General Meeting, Gordon Horsfield and Gerald Wingrove elected to re-invest the net proceeds of their restructuring bonus in the Group through the purchase of 1,729,440 each of the newly converted non-voting shares, at a price of 13.65 pence per share.

Also at the Extraordinary General Meeting on 30 April 2004, a new LTIP was approved by shareholders (note 21). The LTIP plan was, in part, funded by a pool of 4,323,600 of the newly converted non-voting ordinary shares being the total of 7,782,480 non-voting shares referred to above, less the number of shares purchased by Gordon Horsfield and Gerald Wingrove. In May 2004 an Initial Share Award under the LTIP resulted in the purchase of 549,923 shares by certain executive directors, business and team leaders at a price of 13.65 pence per share. The 3,773,677 remaining shares in the LTIP pool were subsequently issued to the LTIP Trustee.

Accordingly, there were 94,254,480 shares of Drax Group Limited in issue as at 31 December 2004, with a nominal value of £943 and a related share premium (which arose on the purchases by Gordon Horsfield and Gerald Wingrove and on the Initial Share Awards) of £0.5 million.

DRAX GROUP PLC

The Company has only one class of ordinary shares, which carry no right to fixed income. No shareholders have waived their rights to dividends. These shares were issued upon Refinancing and Listing as described below.

Pursuant to the schemes of arrangement under which the Refinancing and Listing was implemented, the existing shareholders of Drax Group Limited, including LTIP shareholders, received three ordinary shares of 10 pence each in Drax Group plc in exchange for each share in Drax Group Limited. This resulted in the issue of 282,763,440 ordinary shares in Drax Group plc. Under section 131 of the Companies Act 1985, Drax Group plc qualifies for merger relief to avoid recording a share premium on the shares issued to the existing shareholders of Drax Group Limited. Accordingly, Drax Group plc has recorded these shares within share capital at their nominal value of £28.3 million, with a corresponding debit to share premium of £0.5 million and the merger reserve of £27.8 million to reflect the reverse acquisition adjustment (note 27).

Notes to the Consolidated Financial Statements continued

As described in note 16, A2/A3 Debt holders contributed their A2/A3 Debt in exchange for cash and ordinary shares of 10 pence each in Drax Group plc. A2 Debt holders received 21,668 ordinary shares and £24,421 for each £100,000 of A2 Debt. A3 Debt holders received 28,669 ordinary shares for each £100,000 of A3 Debt. In total A2 Debt holders received cash consideration of £112.0 million and A2/A3 Debt holders received 124,164,221 ordinary shares of 10 pence each in Drax Group plc. Outstanding interest on A2/A3 Debt was repaid in full.

The Group settled the remaining nominal value of A2/A3 Debt, after deduction of the A2 cash consideration, of £433.1 million in exchange for issuing the 124,164,221 ordinary shares in Drax Group plc. The directors determined that the nominal value of A2/A3 Debt approximated its fair value (note 18) by reference to the terms of the debt, principally the ability to prepay at nominal value. The nominal value of shares issued of £12.4 million was therefore lower than the fair value of the asset acquired of £433.1 million. Under section 130 of the Companies Act 1985, the shares are treated as issued fully paid up and the difference of £420.7 million recorded as share premium (note 27).

Accordingly, in total there were 406,927,661 ordinary shares of 10 pence each in Drax Group plc issued and fully paid up as at 31 December 2005, with a nominal value of £40.7 million and related share premium of £420.7 million.

REDEEMABLE SHARES

On 20 October 2005, the Company authorised and issued 499,980 redeemable shares of 10 pence each to Drax Group Limited. These shares were subsequently fully paid up prior to 31 December 2005.

The redeemable shares are not entitled to any dividend or surplus capital return over and above their share issue price of 10 pence. The shares are redeemable at the option of both the Company and the holder and must be redeemed by 20 October 2030. As the shares do not entitle the holder to any residual interest in the Company and are mandatorily redeemable, they are accounted for as debt in accordance with IAS 32.

23. Merger Reserve

	Years ended 31 December	
	2005	2004
	£'m	£'m
At beginning of year	445.1	445.1
Reverse acquisition adjustments:		
– Share for share exchange (note 22)	(27.8)	–
– Transfer of capital reserve (note 24)	293.5	–
At end of year	710.8	445.1

24. Capital Reserve

	Years ended 31 December	
	2005	2004
	£'m	£'m
At beginning of year	293.5	293.5
Reverse acquisition adjustment	(293.5)	–
At end of year	–	293.5

On the reverse acquisition of Drax Group plc by Drax Group Limited, the capital reserve was transferred to the merger reserve.

25. Hedge Reserve

	Years ended 31 December	
	2005	2004
	£'m	£'m
At beginning of year	–	–
Fair value losses on cash flow hedges	(109.7)	–
Deferred tax recognised on fair value losses on cash flow hedges	32.9	–
At end of year	(76.8)	–

The Group enters into short and medium term forward electricity sales contracts to hedge generation output. The Group also purchases coal from a range of domestic and international suppliers. For the purposes of IAS 39, from 1 July 2005, the Group has put in place appropriate hedge accounting documentation to enable it to achieve hedge accounting for a large proportion of its commodity contracts. As a result, mark-to-market movements on contracts which are now considered to be effective hedges are recognised through the hedge reserve. For the period from 1 January 2005 to 30 June 2005, mark-to-market movements on these contracts were reflected directly in the income statement, as appropriate hedge documentation had not been put in place.

26. Retained Losses

	Years ended 31 December	
	2005	2004
	£'m	£'m
At beginning of year	(1,173.2)	(1,162.4)
Profit / (loss) for the year	282.4	(6.5)
Actuarial losses on defined benefit pension schemes	(8.2)	(6.1)
Deferred tax on actuarial losses on defined benefit pension schemes	2.5	1.8
Initial recognition of net mark-to-market liability on adoption of IAS 32 and IAS 39	(5.6)	-
Deferred tax recognised on adoption of IAS 32 and IAS 39	1.7	-
LTIP – credit to equity for share-based payments (note 21)	25.2	-
At end of year	(875.2)	(1,173.2)

27. Shareholders' Funds and Statement of Changes in Shareholders' Equity

	Share capital	Share premium	Merger reserve	Capital reserve	Hedge reserve	Retained losses	Total
	£'m	£'m	£'m	£'m	£'m	£'m	£'m
At 1 January 2004	-	-	445.1	293.5	-	(1,162.4)	(423.8)
Loss for the year	-	-	-	-	-	(6.5)	(6.5)
Actuarial losses on defined benefit pension schemes	-	-	-	-	-	(6.1)	(6.1)
Deferred tax on actuarial losses on defined benefit pension schemes	-	-	-	-	-	1.8	1.8
LTIP – proceeds on shares issued (note 21)	-	0.5	-	-	-	-	0.5
At 31 December 2004	-	0.5	445.1	293.5	-	(1,173.2)	(434.1)
Profit for the year	-	-	-	-	-	282.4	282.4
Actuarial losses on defined benefit pension schemes	-	-	-	-	-	(8.2)	(8.2)
Deferred tax on actuarial losses on defined benefit pension schemes	-	-	-	-	-	2.5	2.5
Initial recognition of net mark-to-market liability on adoption of IAS 32 and 39	-	-	-	-	-	(5.6)	(5.6)
Deferred tax recognised on adoption of IAS 32 and 39	-	-	-	-	-	1.7	1.7
Fair value losses on cash flow hedges	-	-	-	-	(109.7)	-	(109.7)
Deferred tax recognised on fair value losses on cash flow hedges	-	-	-	-	32.9	-	32.9
Share capital issued on Refinancing and Listing	40.7	-	-	-	-	-	40.7
Share premium arising on Refinancing and Listing	-	420.7	-	-	-	-	420.7
Reverse acquisition adjustments:							
- Share for share exchange (note 22)	-	(0.5)	(27.8)	-	-	-	(28.3)
- Transfer of capital reserve (note 24)	-	-	293.5	(293.5)	-	-	-
LTIP – credit to equity for share-based payments (note 21)	-	-	-	-	-	25.2	25.2
At 31 December 2005	40.7	420.7	710.8	-	(76.8)	(875.2)	220.2

Notes to the Consolidated Financial Statements continued

28. Cash Flow from Operating Activities

	Years ended 31 December	
	2005 £'m	2004 £'m
Continuing operations		
Profit / (loss) for the year	282.4	(6.5)
Adjustments for:		
Interest payable and similar charges	114.4	101.2
Interest receivable	(23.5)	(4.6)
Tax credit	(18.8)	(35.1)
Depreciation	31.0	33.0
Reversal of impairment of tangible fixed assets	(19.0)	-
Loss on disposal of property, plant and equipment	0.2	2.0
Unrealised losses on derivative contracts	117.0	-
LTIP – credit to equity for share-based payments	25.2	-
Operating cash flows before movement in working capital	508.9	90.0
Changes in working capital:		
Increase in inventories	(22.6)	(9.8)
Increase in receivables	(123.4)	(9.6)
Increase in payables	99.8	1.0
Increase in pensions	-	1.4
(Decrease) / increase in provisions	(0.4)	0.4
Cash generated from operations	462.3	73.4

29. Employees and Directors

STAFF COSTS (INCLUDING EXECUTIVE DIRECTORS) FOR THE GROUP

	Years ended 31 December	
	2005 £'m	2004 £'m
Included in other operating expenses excluding exceptional items (note 6):		
Wages and salaries	22.4	21.4
Social security costs	2.3	1.8
Other pension costs (note 30)	3.9	3.2
Termination benefits	0.5	-
	29.1	26.4
Included in exceptional other operating expenses (note 21):		
LTIP expenses arising on share-based payment transactions	25.2	-
LTIP expenses arising on cash-based payment transactions	4.7	-
Social security costs arising on share and cash-based payment transactions	7.7	-
	37.6	-

AVERAGE MONTHLY NUMBER OF PEOPLE (INCLUDING EXECUTIVE DIRECTORS) EMPLOYED

	Years ended 31 December	
	2005 Number	2004 Number
Operations	464	475
Business services	124	65
	588	540

30. Pensions

The Group operates an approved defined benefit scheme, on behalf of the Drax Power Group of the Electricity Supply Pension Scheme ("DPG ESPS"). This scheme was closed to new members as from 1 January 2002 unless they qualify through being existing members of another part of the ESPS. The Group also operates a defined contribution scheme.

DEFINED BENEFIT PLANS

The most recent actuarial valuation of the DPG ESPS was 31 March 2004. This has been updated as at 31 December 2005 to reflect relevant changes in assumptions. The principal assumptions made by the actuaries were:

	Years ended 31 December	
	2005 % p.a	2004 % p.a
Discount rate	4.7	5.3
Inflation assumption	2.9	2.9
Rate of increase in pensions in payment and deferred pensions	2.9	3.0
Rate of increase in pensionable salaries	4.4	4.4
Expected return on plan assets	7.0	7.6

The amounts recognised in the balance sheet are determined as follows:

	As at 31 December	
	2005 £'m	2004 £'m
Present value of funded obligations	107.0	85.0
Fair value of plan assets	(62.3)	(48.5)
Net liability recognised in the balance sheet	44.7	36.5

The amounts recognised in the income statement, entirely within other operating expenses, are as follows:

	Years ended 31 December	
	2005 £'m	2004 £'m
Current service cost	2.8	2.5
Interest cost	4.5	3.9
Expected return on plan assets	(3.8)	(3.4)
Total included in staff costs (note 29)	3.5	3.0

The actual return on plan assets was £10.7 million (2004: return £4.8 million).

The amounts recognised in the statement of recognised income and expenditure are as follows:

	Years ended 31 December	
	2005 £'m	2004 £'m
Opening cumulative actuarial losses on defined benefit pension schemes	(22.8)	(16.7)
Actuarial losses on defined benefit pension schemes recognised in the year	(8.2)	(6.1)
Cumulative losses recognised in statement of recognised income and expenditure	(31.0)	(22.8)

Changes in the present value of the defined benefit obligation are as follows:

	Years ended 31 December	
	2005 £'m	2004 £'m
Opening defined benefit obligation	85.0	71.9
Service cost	2.8	2.5
Employee contributions	0.8	0.7
Interest cost	4.5	3.9
Actuarial losses	15.1	7.6
Benefits paid	(1.2)	(1.6)
Closing defined benefit obligation	107.0	85.0

Notes to the Consolidated Financial Statements continued

Changes in the fair value of plan assets are as follows:

	Years ended 31 December	
	2005	2004
	£'m	£'m
Opening fair value of plan assets	48.5	42.9
Expected return	3.8	3.4
Actuarial gains	6.9	1.5
Employer contributions	3.5	1.6
Employee contributions	0.8	0.7
Benefits paid	(1.2)	(1.6)
Closing fair value of plan assets	62.3	48.5

The major categories of plan assets as a % of total plan assets are as follows:

	Years ended 31 December	
	2005	2004
	%	%
Equities	95.3	99.8
Fixed interest bonds	4.7	-
Cash	-	0.2

The pension plan assets do not include any ordinary shares issued by Drax Group plc or any property occupied by Drax Group plc.

The history of experience adjustments is as follows:

	Years ended 31 December			
	2005	2004	2003	2002
	£'m	£'m	£'m	£'m
Defined benefit obligation	(107.0)	(85.0)	(71.9)	(60.8)
Plan assets	62.3	48.5	42.9	35.6
Deficit	(44.7)	(36.5)	(29.0)	(25.2)
Experience adjustments on plan liabilities	(15.1)	(7.6)	(6.7)	(2.1)
Experience adjustments on plan assets	6.9	1.5	4.1	(12.0)

DEFINED CONTRIBUTION PLANS

Pension costs for the defined contribution scheme are as follows:

	Years ended 31 December	
	2005	2004
	£'m	£'m
Total included in staff costs (note 29)	0.4	0.2

The Group expects to contribute £4.3 million to its pension plans during the 12 months ended 31 December 2006.

31. Capital and Other Financial Commitments

	As at 31 December	
	2005	2004
	£'m	£'m
Contracts placed for future capital expenditure not provided in the financial statements	19.1	0.3
Future commitments to purchase coal	736.6	880.9
Future commitments to sell power	920.7	520.1

Certain of the future commitments to purchase coal are under variable priced contracts.

32. Related Party Transactions

SUBSIDIARY COMPANIES

The principal Group subsidiary undertakings are disclosed in note 3 to the Company's separate financial statements which follow these consolidated financial statements. Transactions between subsidiaries and between the holding company and its subsidiaries are eliminated on consolidation.

REMUNERATION OF KEY MANAGEMENT PERSONNEL

The remuneration of the directors, 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 Report on pages 34 to 41.

	Years ended 31 December	
	2005 £'000	2004 £'000
Salaries and short-term benefits	1,487	955
Termination benefits	469	-
Aggregate emoluments	1,956	955
Aggregate amounts receivable under long-term incentive schemes	6,906	-
Company contributions to money purchase pension schemes	159	38
	9,021	993

Amounts receivable under long-term incentive schemes represent cash and share-based payments under the LTIP. The expense arising from share-based payments included in the income statement and in the table above has been determined based on the fair value of the related Performance Share Awards at the date of grant (note 21).

There were no other transactions with directors for the periods covered by these consolidated financial statements.

33. Principal Subsidiaries

A list of the significant investments in subsidiaries, including the name, country of incorporation and proportion of ownership interest is given in note 3 to the Company's separate financial statements which follow these consolidated financial statements.

InPower Limited (Jersey), InPower 2 Limited (Jersey), NoteCo Limited (Jersey) and BondPower Limited (Jersey) were all incorporated in Jersey. Although not subsidiaries of Drax Group plc, they have been consolidated in the financial statements in accordance with SIC 12 "Consolidation - Special Purpose Entities" on the basis that their sole purpose was to hold the debt of the Group prior to the Refinancing and Listing on 15 December 2005.

34. Reconciliation of Net Assets and Profit under UK GAAP to IFRS

The following tables show the impact of IFRS on the consolidated income statement and cash flow statements for the year ended 31 December 2004 as well as the impact on net assets at 1 January 2002, being the Group's date of transition to IFRS, and 31 December 2004.

CONSOLIDATED BALANCE SHEET AS AT 1 JANUARY 2002

	UK GAAP £m	IAS 12 Income taxes £m	IAS 19 Employee benefits £m	IAS 16 Property, plant and equipment £m	Total IFRS adjustments £m	IFRS £m
Non-current assets						
Property, plant and equipment	1,140.3	-	-	(8.2)	(8.2)	1,132.1
Intangible assets	583.4	-	-	-	-	583.4
Total non-current assets	1,723.7	-	-	(8.2)	(8.2)	1,715.5
Current assets	317.5	-	-	-	-	317.5
Current liabilities	(150.0)	-	-	-	-	(150.0)
Non-current liabilities	(1,387.1)	(293.0)	(7.3)	2.5	(297.8)	(1,684.9)
Net assets	504.1	(293.0)	(7.3)	(5.7)	(306.0)	198.1
Issued equity	445.1	-	-	-	-	445.1
Retained losses	59.0	(293.0)	(7.3)	(5.7)	(306.0)	(247.0)
Total shareholders' equity	504.1	(293.0)	(7.3)	(5.7)	(306.0)	198.1

Notes to the Consolidated Financial Statements continued

CONSOLIDATED BALANCE SHEET AS AT 31 DECEMBER 2004

	UK GAAP £m	IAS 12 Income taxes £m	IAS 19 Employee benefits £m	IAS 16 Property, plant and equipment £m	IAS 38 Goodwill/ IAS 36 impairment £m	Total IFRS adjustments £m	IFRS £m
Non-current assets							
Property, plant and equipment	1,041.0	-	-	(12.4)	9.1	(3.3)	1,037.7
Current assets	190.4	-	-	-	-	-	190.4
Current liabilities	(275.6)	-	1.5	-	-	1.5	(274.1)
Non-current liabilities	(1,102.2)	(260.9)	(26.0)	3.7	(2.7)	(285.9)	(1,388.1)
Net liabilities	(146.4)	(260.9)	(24.5)	(8.7)	6.4	(287.7)	(434.1)
Issued equity	-	-	-	-	-	-	-
Share premium	0.5	-	-	-	-	-	0.5
Merger reserve	445.1	-	-	-	-	-	445.1
Capital reserve	293.5	-	-	-	-	-	293.5
Retained losses	(885.5)	(260.9)	(24.5)	(8.7)	6.4	(287.7)	(1,173.2)
Total shareholders' equity	(146.4)	(260.9)	(24.5)	(8.7)	6.4	(287.7)	(434.1)

CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2004

	UK GAAP £m	Reclass- ification £m	IAS 12 Income taxes £m	IAS 19 Employee benefits £m	IAS 16 Property, plant and equipment £m	Total IFRS adjustments £m	IFRS £m
Revenue	549.3	74.8	-	-	-	74.8	624.1
Fuel costs	(309.9)	(74.8)	-	-	-	(74.8)	(384.7)
Other operating expenses	(184.6)	-	-	0.1	(2.4)	(2.3)	(186.9)
Other income	2.5	-	-	-	-	-	2.5
Operating profit	57.3	-	-	0.1	(2.4)	(2.3)	55.0
Interest payable and similar charges	(101.2)	-	-	-	-	-	(101.2)
Interest receivable	4.6	-	-	-	-	-	4.6
Loss before tax	(39.3)	-	-	0.1	(2.4)	(2.3)	(41.6)
Tax credit	26.7	-	7.7	-	0.7	8.4	35.1
Loss for the year	(12.6)	-	7.7	0.1	(1.7)	6.1	(6.5)

CONSOLIDATED CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2004

	UK GAAP £m	IAS 12 Income taxes £m	IAS 19 Employee benefits £m	IAS 16 Property, plant and equipment £m	Total IFRS adjustments £m	IFRS £m
Loss for the year	(12.6)	7.7	0.1	(1.7)	6.1	(6.5)
Adjustments for:						
Interest payable and similar charges	101.2	-	-	-	-	101.2
Interest receivable	(4.6)	-	-	-	-	(4.6)
Tax credit	(26.7)	(7.7)	-	(0.7)	(8.4)	(35.1)
Depreciation	32.1	-	-	0.9	0.9	33.0
Loss on disposal of property, plant and equipment	0.5	-	-	1.5	1.5	2.0
Operating cash flows before movements in working capital	89.9	-	0.1	-	0.1	90.0
Increase in inventories	(9.8)	-	-	-	-	(9.8)
Increase in receivables	(9.6)	-	-	-	-	(9.6)
Increase in payables	1.0	-	-	-	-	1.0
Increase in pensions	-	-	1.4	-	1.4	1.4
Increase in provisions	0.4	-	-	-	-	0.4
Cash generated from operations	71.9	-	1.5	-	1.5	73.4

IAS 19 EMPLOYEE BENEFITS

Under IFRS, the Group applies IAS 19. Under UK GAAP, the Group applied the provisions of SSAP 24 "Accounting for Pension Costs" and also provided detailed disclosures under FRS 17 "Retirement Benefits". IAS 19 follows a balance sheet approach which is similar to that of FRS 17.

Under IAS 19, the pension scheme deficit in respect of the approved defined benefit pension plan is recognised on the balance sheet. The income statement expense comprises the current service cost, the interest cost, the expected return on any plan assets and the appropriate portion of any past service costs. Actuarial gains and losses are recognised in full in the period in which they arise in the statement of recognised income and expenditure.

The Group has taken advantage of the IFRS 1 exemption allowing full actuarial losses to be recognised at the date of transition.

The balance sheet impact of the implementation of this policy is to recognise an increased pension liability of £10.5 million in the Group's opening IFRS balance sheet at 1 January 2002 and an increased pension liability of £36.5 million in the Group's IFRS balance sheet as at 31 December 2004 (both before tax). During the year ended 31 December 2004 an additional amount of £0.1 million (before tax) was credited to the income statement.

IFRS 2 SHARE-BASED PAYMENTS

Under IFRS, the Group applies IFRS 2. Under IFRS 2, a charge is required for all share-based payments including share options. The charge in the income statement is based on the fair value of the shares or options at grant date. The charge to the income statement is recognised over the relevant vesting periods, adjusted to reflect actual and expected levels of vesting. The fair value of share-based payments under the Group's LTIP have been calculated based on the implied fair value of the equity at the date of grant. Under UK GAAP, the income statement charge, if any, is based on the difference between exercise price and the market price on the date of issue.

The Group has taken advantage of the IFRS 1 exemption to only apply IFRS 2 to awards granted since Exposure Draft 2 was issued on 7 November 2002 and which have not vested by 31 December 2004.

IAS 16 PROPERTY, PLANT AND EQUIPMENT

Under IFRS, the Group applies IAS 16. Under IAS 16 each significant part of an item of property, plant and equipment should be depreciated separately, and the useful life, residual values and depreciation method used is required to be reviewed at least each financial year end, with any revisions in these estimates being taken prospectively.

Following a detailed exercise to review all estimated useful lives of the individually significant items of plant and machinery, the Group identified a number of items with estimated useful lives of less than the estimated life of the station. This resulted in an adjustment of £8.2 million (before tax) to reduce the net book value of property, plant and equipment in the Group's opening IFRS balance sheet at 1 January 2002, and additional depreciation charges of £0.9 million per annum thereafter. The balance sheet impact at 31 December 2004 of the implementation of this policy is to reduce the book value of property, plant and equipment by £12.4 million before tax.

IAS 12 INCOME TAXES

Under UK GAAP, deferred tax is provided based on timing differences between accounting and taxable profits. Under IFRS deferred tax is required to be provided on all temporary differences between the book carrying values of assets and liabilities and their related tax bases.

Following the acquisition of the power station from National Power in 1999, for UK GAAP purposes the Group has treated differences between the book value of non-qualifying tangible fixed assets and their tax bases as permanent items for the purposes of deferred tax and accordingly, no deferred tax liability has been recorded. Under IAS 12, such differences are treated as temporary timing differences and hence an additional deferred tax liability of £293.0 million has been recorded in the Group's opening IFRS balance sheet as at 1 January 2002. To the extent that depreciation has been charged in following years this deferred tax liability has reduced, with a corresponding credit recognised in the tax charge in the income statement.

This provision does not affect the Group's underlying tax position nor give rise to any expected future liabilities to pay tax.

IMPACT OF IAS 32 AND IAS 39

The Group has adopted IAS 32 and IAS 39 from 1 January 2005. IAS 32 and IAS 39 set out the accounting rules surrounding the recognition, measurement, disclosure and presentation of financial instruments. The Group's accounting policies under IAS 32 and IAS 39 will not be impacted by the elements carved out of the EU endorsement, and hence will comply in full with IAS 39.

The most significant impacts of adopting these standards are set out below:

Commodity contracts – The Group enters into short and medium term forward electricity contracts for the sale of electricity and the purchase of coal and carbon emissions allowances. Due to the nature of some of these contracts and the way they are managed, the own use exemption within IAS 39 has only been applied to a limited number of them. From 1 July 2005,

Notes to the Consolidated Financial Statements continued

the Group has put in place appropriate hedge accounting documentation to enable it to achieve hedge accounting for a large proportion of its commodity contracts. As a result, mark-to-market movements on contracts which are now considered to be effective hedges are recognised through the hedge reserve. For the period from 1 January 2005 to 30 June 2005, mark-to-market movements on these contracts were reflected directly in the income statement, as appropriate hedge documentation had not been put in place.

Interest rate swaps – The Group enters into interest rate swap arrangements to hedge variable interest costs on debt. From 1 July 2005, the Group has put in place appropriate hedge accounting documentation to enable it to achieve hedge accounting for these arrangements. As a result, mark-to-market movements on arrangements which are now considered to be effective hedges are recognised through the hedge reserve. For the period from 1 January 2005 to 30 June 2005, mark-to-market movements on these contracts were reflected directly in the income statement, as appropriate hedge documentation had not been put in place.

Embedded derivatives – IAS 39 requires that all embedded derivatives are identified, and where relevant, separated from the host contract and separately valued. The Group have completed a review of all contracts for embedded derivatives and consider all embedded derivatives to be closely related to the economic characteristics and risks of the host contract. As such, no embedded derivatives have been separately valued.

CASH FLOW STATEMENT

The consolidated cash flow statement prepared in accordance with UK GAAP (FRS 1 "Cash flow statements (Revised)") presented substantially the same information that is required under IFRS (IAS 7 "Cash flow statements"). However under IFRS there are differences with regard to the definition of cash and cash equivalents and with regards to the classification of items within the cash flow statement.

Under IFRS, cash and cash equivalents includes short-term deposits which under UK GAAP were included within the management of liquid resources category.

Under UK GAAP, cash flows were reported under nine standard headings; operating activities, dividends from joint ventures and associates, returns on investments and servicing of finance, taxation, capital expenditure and financial investments, acquisitions and disposals, equity dividends paid, management of liquid resources and financing. Under IFRS the cash flows are classified under three standard headings; operating activities, investing activities and financing activities.

Income taxes paid or received in the period are classified as a part of operating cash flows under IFRS, but were included in a separate category of tax cash flow under UK GAAP.

RECLASSIFICATION

In the Group's historical financial statements revenue has been recorded net of bilateral power 'buy-backs' (i.e. the cost of power purchased to meet power sale commitments). In addition, the Group's activities in the balancing mechanism have been included within revenue irrespective of whether the net result from those activities is income or expense.

In these consolidated financial statements, and in accordance with common industry practice, the Group has recorded a reclassification in each reporting period to reflect revenue and fuel costs for the total of bilateral power buy-backs and any balancing mechanism net expense. Where the result from the balancing mechanism is net income for the period, no reclassification is required.

Independent Auditors' Report to the Company

We have audited the individual company financial statements of Drax Group plc for the period ended 31 December 2005 which comprise the balance sheet and the related notes 1 to 8. These individual company financial statements have been prepared under the accounting policies set out therein.

The corporate governance statement and the directors' remuneration report are included in the group annual report of Drax Group plc for the year ended 31 December 2005. We have reported separately on the group financial statements of Drax Group plc for the year ended 31 December 2005 and on the information in the directors' remuneration report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective Responsibilities of Directors and Auditors

The directors' responsibilities for preparing the annual report and the individual company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the individual company financial statements in accordance with relevant United Kingdom legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the individual company financial statements.

Basis of Audit Opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the individual company financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the individual company financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion:

- the individual company financial statements give a true and fair view,
- in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2005; and
- the individual company financial statements have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors
London
7 March 2006

Company Balance Sheet

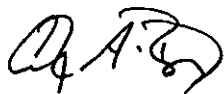
	As at 31 December	
	Notes	2005 £'000
Fixed assets		
Investment in subsidiaries	3	461,368
Current assets		
Cash at bank and in hand	4	50
Net current assets		50
Total assets less current liabilities		461,418
Creditors: Amounts falling due after more than one year		
Redeemable shares	8	(50)
Net assets		461,368
Capital and reserves		
Called-up share capital	5	40,693
Share premium account	6	420,675
Total equity shareholders' funds	7	461,368

These financial statements were approved by the Board of directors on 7 March 2006.

Signed on behalf of the Board of directors.



Dorothy Thompson
Chief Executive



Gordon Boyd
Finance Director

Notes to the Company Balance Sheet

1. Significant Accounting Policies

The separate financial statements of the Company are presented as required by the Companies Act 1985. They have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards and law.

The principal accounting policies are summarised below. They have all been applied consistently since incorporation of the Company on 13 September 2005.

CASH FLOW STATEMENT

The cash flows of the Group are included in the consolidated cash flow statements of Drax Group plc, whose accounts are publicly available. Accordingly, the Company has taken advantage of the exemption under FRS 1 "Cash Flow Statements" not to publish a cash flow statement.

RELATED PARTY TRANSACTIONS

The Company has taken advantage of the exemption granted by paragraph 3(c) of FRS 8 "Related Party Disclosures" not to disclose transactions with other group companies.

FIXED ASSET INVESTMENTS

Fixed asset investments in subsidiaries are stated at cost less, where appropriate, provision for impairment.

2. Profit and Loss Account

As permitted by section 230 of the Companies Act 1985, 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 7 March 2006. Drax Group plc reported a profit for the period ended 31 December 2005 of £nil.

The auditors' remuneration for audit services to the Company was borne by a subsidiary undertaking.

The Company has no employees other than the directors, whose remuneration was borne by a subsidiary undertaking.

3. Fixed Asset Investments

	Subsidiary undertakings
	£'000
Cost	
Additions	461,368
At 31 December 2005	461,368

As permitted by section 231 of the Companies Act 1985 the Company has elected to present only its principal subsidiary undertakings.

PRINCIPAL SUBSIDIARY UNDERTAKINGS

Name and nature of business	Country of incorporation and registration	Type of share	Group effective shareholding
Drax Finance Limited (holding company)	England and Wales	Ordinary	100%
Drax Group Limited (holding company)*	Cayman Islands	Ordinary	100%
Drax Intermediate Holdings Limited (holding company)*	Cayman Islands	Ordinary	100%
Drax Holdings Limited (holding company)*	Cayman Islands**	Ordinary	100%
Drax Electric Limited (holding company)*	Cayman Islands	Ordinary	100%
Drax Limited (holding company)*	Cayman Islands	Ordinary	100%
Drax Power Limited (power generation)*	England and Wales	Ordinary	100%
Drax Ouse Limited (dormant company)*	England and Wales	Ordinary	100%
Drax Investments Limited (investment company)*	England and Wales	Ordinary	100%

All subsidiary undertakings operate in their country of incorporation. All subsidiary undertakings have 31 December year ends, except as indicated below.

* Held by an intermediate subsidiary undertaking

** 30 December year end

InPower Limited (Jersey), InPower 2 Limited (Jersey), NoteCo Limited (Jersey) and BondPower Limited (Jersey) were all incorporated in Jersey. Although not subsidiaries of Drax Group plc, they have been included in the Group IFRS consolidated financial statements in accordance with SIC 12 "Consolidation – Special Purpose Entities" on the basis that their sole purpose was to hold the debt of the Group prior to the Refinancing and Listing on 15 December 2005.

Notes to the Company Balance Sheet

continued

4. Cash at Bank and In Hand

	As at 31 December 2005 £'000
Cash at bank and in hand	50

5. Called-up Share Capital

	As at 31 December 2005 £'000
Authorised	
999,500,020 ordinary shares of £0.10 each	99,950
Issued and fully paid	
406,927,661 ordinary shares of £0.10 each	40,693

The Company was incorporated on 13 September 2005 with an authorised share capital of £50,000, comprising 50,000 shares of £1 each. Two ordinary shares were allotted, and fully paid, on incorporation.

Subsequently, on 20 October 2005, the shares were sub-divided into 500,000 shares of 10 pence each.

On 20 October 2005, the authorised share capital was increased from £50,000 to £100,000,000 comprising 1,000,000,000 shares of 10 pence each, through the creation of 999,500,000 ordinary shares.

The Company's ordinary share capital was issued pursuant to the schemes of arrangement which implemented the Group's Refinancing and Listing on 15 December 2005. This included the issue of 124,164,221 ordinary shares to the holders of A2/A3 Debt (in order to settle that debt) and 282,763,440 ordinary shares to the existing shareholders of Drax Group Limited (in exchange for those shares in Drax Group Limited). These transactions are described more fully in note 16 and note 22 of the Group's consolidated financial statements.

6. Share Premium Account

The share premium of £420.7 million arose on Refinancing and Listing when the Group settled the remaining nominal value of A2/A3 debt, after deduction of the A2 cash consideration, of £433.1 million in exchange for issuing ordinary shares in Drax Group plc with a nominal value of £12.4 million. This transaction is described more fully in note 16 and note 22 of the Group's consolidated financial statements.

7. Analysis of Movements in Equity Shareholders' Funds

	Share capital £'000	Share premium £'000	Total £'000
Share capital issued	40,693	420,675	461,368
At 31 December 2005	40,693	420,675	461,368

8. Redeemable Shares

On 20 October 2005, the Company authorised and issued 499,980 redeemable shares of 10 pence each to Drax Group Limited. These shares were subsequently fully paid up prior to 31 December 2005.

The redeemable shares are not entitled to any dividend or surplus capital return over and above their share issue price of 10 pence. The shares are redeemable at the option of both the Company and the holder and must be redeemed by 20 October 2030. As the shares do not entitle the holder to any residual interest in the Company and are mandatorily redeemable, they are accounted for as debt in accordance with FRS 25 "Financial Instruments: Disclosure and Presentation".

Shareholder Information

Group Financial Calendar for 2006

At the date of publication of this document, the following are the proposed key dates in the 2006 financial calendar:

Annual General Meeting	12 May 2006
Trading statement	June 2006
Announcement of unaudited six months' interim results	September 2006
Trading statement	December 2006

Other significant dates, or amendments to the proposed dates above, will be posted on the Company's website as and when they become available.

Share Price

Shareholders can access the current share price of Drax Group plc ordinary shares on the Company's website at www.draxgroup.plc.uk. During 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.

Company Share Registrar and Transfer Office

Shareholders who have a query regarding their shareholding should contact the Company's share registrars at Capita IRG Plc, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU or by telephone on 0870 162 3100 from within the UK, or +44 (0)20 8639 2342 from outside the UK. When contacting the registrar it is advisable to have the investor code to hand and quote Drax Group plc, as well as the name and address in which the shares are held.

Shareholder Profile

The categories of ordinary shareholders and the ranges and size of shareholdings as at 31 December 2005 are set out below:

Analysis of shareholders	No. of Shareholders	%	No. of Shares	%
Private shareholders	207	52.94	7,536,383	1.85
Investment trusts	1	0.26	11,400	0.00
Nominee companies	158	40.41	260,239,378	63.96
Limited companies	9	2.30	7,018,464	1.72
Bank and bank nominees	11	2.81	53,313,527	13.10
Other institutions	5	1.28	78,808,509	19.37
Total	391	100.00	406,927,661	100.00

Range	No. of Shareholders	%	No. of Shares	%
1-5,000	174	44.50	288,673	0.07
5,001-10,000	30	7.67	187,361	0.05
10,001-100,000	82	20.97	3,490,232	0.86
100,001-500,000	41	10.50	11,097,370	2.73
500,001-5,000,000	46	11.76	73,619,759	18.08
5,000,001 and above	18	4.60	318,244,266	78.21
Total	391	100.00	406,927,661	100.00

Company Information and Professional Advisers

Drax Group plc
COMPANY SECRETARY
Peter J Rothwell

REGISTERED OFFICE AND TRADING ADDRESS

Drax Power Station
PO Box 3
Selby
North Yorkshire
YO8 8PQ

Telephone +44 (0)1757 618381
Fax +44 (0)1757 612192

REGISTRATION DETAILS

Registered in England and Wales
Company Number: 5562053

COMPANY WEBSITE

www.draxgroup.plc.uk

AUDITORS

Deloitte & Touche LLP
Stonecutter Court
1 Stonecutter Street
London
EC4A 4TR

SOLICITORS

Norton Rose
Kempson House
Camomile Street
London
EC3A 7AN

BROKERS

Deutsche Bank AG
Winchester House
1 Great Winchester Street
London
EC2N 2DB

Dresdner Kleinwort Wasserstein Limited
PO Box 560
20 Fenchurch Street
London
EC3P 3DB

REGISTRARS

Capita Registrars
Capita IRG Plc
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4TU

FINANCIAL PR

Tulchan Communications Group Limited
Sixth Floor, Kildare House
3 Dorset Rise
London
EC4Y 8EN

Drax Group plc
Drax Power Station
PO Box 3
Selby
North Yorkshire
YO8 8PQ

Telephone +44 (0)1757 618381
Fax +44 (0)1757 612192

www.draxgroup.plc.uk