August 2000

Regulatory Accounts

Consultation Paper

Executive summary

This consultation paper seeks views on the requirements on electricity and gas companies to prepare and publish regulatory accounts. Good quality accounting information is important to the effective regulation of distribution and transmission networks and so helps ensure that customers' interests are properly protected.

Regulatory accounts are the primary source of regular audited financial information about the businesses regulated by Ofgem. At present they comprise accounting information on each of the licensed separate businesses of the successor companies to the privatised electricity and gas companies, and also the Independent Public Gas Transporters. New entrants into electricity generation, electricity and gas supply and gas shipping are not required to prepare regulatory accounts.

At present limited use is made of regulatory accounts by Ofgem and the companies, who view the preparation of regulatory accounts as burdensome in relation to their usefulness. There is evidence that customer representatives look at them, although they too would benefit from more relevant and consistent information. Regulatory accounts are thought of as not being useful because they provide information that is generally of low quality, largely because of a lack of detailed segmental analysis and inconsistencies in cost attributions, allocations and the treatment of inter-business charges. It is the purpose of this review to rationalise and improve regulatory accounts, so that where appropriate they provide better information, which can be published each year, in a standard format, that facilitates comparisons across time and across companies and with the assumptions underlying price controls.

This consultation paper suggests that regulatory accounts should be:

- prepared only by those separate licensed businesses subject to price control;
- prepared on the basis of historical cost accounting principles but with disclosure of each company's estimate of its regulatory asset value;
- presented in such a way so that they can be reconciled in a reasonably straightforward way with the assumptions underlying the price control and the statutory accounts;

- subject to a more rigorous audit process; and

- published annually and include more information and narrative.

Responses to this paper should arrive no later than 5 October 2000.

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1 Introduction

Background

1.1 This consultation paper discusses the requirements on electricity and gas companies to prepare and publish regulatory accounts. Good quality accounting information is important to the effective regulation of distribution and transmission networks and so helps ensure that customers' interests are properly protected.

1.2 Regulatory accounts are the primary source of regular audited financial information about the businesses regulated by Ofgem. At present they comprise accounting information on each of the licensed separate businesses of the successor companies to the privatised electricity and gas companies, and also the Independent Public Gas Transporters (IPGTs). New entrants into electricity generation, electricity and gas supply and gas shipping are not required to prepare regulatory accounts.

1.3 For each of the companies that prepare regulatory accounts, the main rules governing the preparation of these accounts are set out in licence conditions. In broad terms these rules require that the licensee must keep separate accounting records for each separate business in the form that would be required by the Companies Act 1985 if the separate businesses were separate companies. Licensees must prepare regulatory accounts for each separate business, including profit and loss account, balance sheet and cash flow statements. The accounts are audited by each licensee's external auditors.

1.4 The Office of Electricity Regulation (OFFER) published a consultation paper on regulatory accounts in October 1998 (which is available on Ofgem's website www.ofgem.gov.uk). This paper described the main issues relating to regulatory accounts in the electricity industry and provided a detailed description of the existing arrangements. A summary of the responses to this paper is included in appendix 1.

1.5 It will be necessary to ensure that any changes to existing licence conditions do not create inconsistencies with the EU Directives on the internal markets for electricity and gas. Nevertheless, the implementation of these Directives is a matter for Government and not Ofgem.

1.6 In addition to regulatory accounts those licensees owning distribution and or transmission networks have obligations with respect to financial ring-fencing and business separation, which require, among other things, the companies controlling these businesses to safeguard their financial wellbeing. While these obligations have sometimes been added to the licence conditions relating to regulatory accounts they are not part of this review.

1.7 An Inter-Regulatory Working Group is also examining regulatory accounting issues and will publish a consultation paper on cross-industry issues in due course. That consultation paper will summarise the approaches adopted by different utility regulators, discuss consistency of approach and where appropriate make suggestions for greater co-ordination between regulatory offices.

1.8 This chapter provides an introduction and background. Chapter 2 describes the scope of the existing regulatory arrangements and discusses which electricity and gas businesses should produce regulatory accounting information in the future. Chapter 3 describes some of the changes that will be necessary to improve the quality of information in regulatory accounts. Issues relating to the audit of regulatory accounts are dealt with in chapter 4. Other matters, such as issues relating to publication and the provision of narrative are dealt with in chapter 5. Appendix 1 provides a summary of the responses to the October 1998 consultation paper. Appendix 2 sets out a draft template for electricity distribution regulatory accounts.

Present Arrangements in the Electricity and Gas Industries

1.9 Tables 1A and 1B below show the electricity and gas licensees presently required to prepare regulatory accounts and the separate businesses applicable to each.

TABLE 1A: COMPANIES PREPARING REGULATORY ACCOUNTS IN THE ELECTRICITY INDUSTRY

Companies	***Businesses***
Regional Electricity Companies	Distribution Supply Second Tier Supply Generation
Scottish Power, Scottish Hydro	Transmission Distribution Supply Second Tier Supply Generation Wholesaling
National Power, PowerGen, First Hydro	Second Tier Supply Generation
British Energy, BNFL	Second Tier Supply Nuclear Generation Non Nuclear Generation
National Grid Company	Transmission Settlements Interconnectors Ancillary Services

TABLE 1B: COMPANIES PREPARING REGULATORY ACCOUNTS IN THE GAS INDUSTRY

Companies	***Businesses***
Centrica	Supply Shipping
BG Transco	Transportation(1) Storage
IPGTs	Distribution

(1) Gas transportation presently encompasses both distribution and transmission activities.

1.10 Electricity and gas companies prepare interim and annual regulatory accounts. The interim accounts have never been specified in detail, which has resulted in a minimum of information being included in them. In addition, the Public Electricity Suppliers (PESs) also produce an annual return of additional information in an electronic format.

1.11 The regulatory accounts published by electricity companies exclude certain information, such as cost allocation statements, and aggregate certain other information, such as that relating to first and second tier electricity supply activities. At present not all gas companies are required to publish their regulatory accounts, although most gas companies do publish some regulatory accounting information.

Rationale for the Review

1.12 The review of regulatory accounts will consider the requirements on companies to prepare regulatory accounts and publish accounting information. Where appropriate, proposals will be made to increase transparency and improve regulatory effectiveness. Where regulatory accounts are no longer required the review will provide an opportunity to rationalise regulatory accounting arrangements and reduce the regulatory burden on companies.

1.13 At present limited use is made of regulatory accounts by Ofgem, or the companies, who view the preparation of regulatory accounts as burdensome in relation to their usefulness. There is evidence that customer representatives look at them, although they too would benefit from more relevant and consistent information. Regulatory accounts are thought of as not being useful because they provide information that is generally of low quality, largely because of a lack of detailed segmental analysis and inconsistencies in cost attributions, allocations and inter-business charging.

1.14 It is the purpose of this review to rationalise and improve regulatory accounts, so that where appropriate they will provide better information, which can be published each year, in a standard format, that facilitates comparisons across time and across companies and with the assumptions underlying price controls.

1.15 This review has no direct impact on customers, although they will benefit from the increased transparency of accounting information, which will assist with the effective regulation of the monopoly activities of licence holders. The impact on the industry in terms of increased costs is not yet clear. This will be considered in formulating final proposals and it will be important that any additional costs are proportionate when compared to the advantages of increased transparency and regulatory effectiveness.

1.16 The review of regulatory accounts is included in Ofgem's plan and budget for 2000/01, which was published in March 2000 and is available on Ofgem's website. The direct costs to Ofgem of this review in 2000/01 will be approximately £0.4 million. These will mainly relate to the use of consultants that will assist in developing new cost attribution and allocation guidelines for the electricity distribution sector.

1.17 As well as improving the provision and transparency of financial information, the project should reduce the costs and improve the effectiveness of future price control reviews, as less time and effort will be required in analysing and adjusting accounting data. In addition the review of regulatory accounts has close links with the information and incentives project (IIP).

Timetable

1.18 Following consideration of the responses to this paper final proposals will be published in November 2000 for new arrangements to take effect for the year commencing April 2001. Revised cost attribution and allocation guidelines will also be put in place for electricity distribution for the year commencing April 2001. Similar guidelines will be developed for each of NGC's transmission business and Transco's transportation business following completion of the present price control reviews relating to these businesses, and for the Scottish electricity transmission businesses.

Responding to this document

1.19 It would be helpful to hear from all those with an interest in the issues raised in this paper, including customers, their representatives and the companies. Views are invited by 5 October. Responses (preferably by e-mail) should be sent to:

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1.20 Responses will be published by placing them in the Ofgem library.

2 The Scope of Regulatory Accounting Arrangements

Introduction

2.1 The existing regulatory accounting requirements have been in place for a number of years. In electricity the arrangements have remained largely unchanged since privatisation. In gas there have been changes, in particular following the 1993 MMC report that required the separation of transportation and storage activities from the trading activities of British Gas. Over this time there have been significant changes in the structure of the electricity and gas industries and in regulatory policy. These changes have encompassed the way many licensees organise and manage their businesses, changes in ownership and the development of proposals for business separation and financial ring-fencing. Another important change has been the development of competition in electricity generation and electricity and gas supply and gas shipping. In the light of these developments it is appropriate to consider the future purpose and form of regulatory accounting requirements.

2.2 Regulatory accounts provide regular audited financial information about regulated businesses, for use by the regulator and the wider public. This has the potential to inform price control reviews, facilitate regular assessment of each company's progress and condition, and could provide a basis for examining competition issues. In the light of these considerations applications of regulatory accounting information might include:

- monitoring performance against the assumptions underlying existing price controls;
- informing future price control reviews;
- helping detect anti-competitive behaviour including cross-subsidy and discrimination; and
- securing the financial health of a business.

2.3 However, in order to achieve any of these objectives the regulatory accounts would need to contain high quality information that is consistent across time and companies.

Monitoring Performance and Informing Price Control Reviews

2.4 At present regulatory accounts do not include the information necessary to make proper comparisons between actual performance and the assumptions underlying network price controls. The reasons for this relate to difficulties with the present format of the regulatory accounts, the cost attribution and allocation guidelines, the co-ordination of reporting periods and the basis of accounting. The most problematic issues relate to the guidelines on cost attributions, allocations and inter-business charging, and these are summarised below. All these matters are dealt with in detail in chapter 3.

2.5 For some businesses, particularly electricity distribution, the existing guidelines on cost attribution and allocation (known as CSC 194) are not consistent with the revised arrangements for business separation and distribution price control introduced from April 2000. The price control review revealed that CSC 194 allowed the costs of certain activities to be allocated on the basis of somewhat arbitrary assumptions rather than attributed using appropriate cost drivers. In addition certain PESs were tending to capitalise a wider range of costs, reducing operating costs and increasing capital expenditure. The price control review also highlighted an increasing trend for companies to use service units, outside the distribution business but within the wider corporate group, to provide services and make recharges to the distribution business. These recharges appeared to inflate distribution business costs and transfer profits to elsewhere in the group. In order to deal with these difficulties substantial adjustments were necessary to normalise data across distribution businesses. For other regulated businesses the guidelines on cost attributions and allocations are also inadequate.

2.6 In the light of these factors it is not straightforward to assess the underlying costs of regulated businesses or whether companies are achieving the efficiency targets implicit in a price control. This has the following consequences:

- customers and their representatives feel disenfranchised, as they have no way of accurately mapping how a company's operational performance relates to its financial results or how it is performing against the assumptions underlying its price control;

- investors may feel that by not being able to determine how a company is performing against the assumptions underlying its price control increases uncertainty. Therefore, new regulatory accounting arrangements should reduce regulatory risk as there will be less uncertainty relating to factors such as cost allocation and inter-business charging. In the longer term this should reduce the cost of capital and lead to lower prices for customers; and

- Ofgem does not receive regular financial information of sufficient quality to facilitate the monitoring of the performance of those companies subject to network price controls or compile financial information for future price control reviews. This has led to an undue emphasis on the periodic review process with Ofgem needing to collect and analyse a disproportionate amount of information at the time of a price control review. The importance for companies of the proposals and their ability to influence the outcome of the review in favour of their shareholders may have led to a disproportionate amount of management time and effort being devoted to this process, with certain companies engaging in a form of regulatory gaming. This is not in the interests of customers.

2.7 In order to deal with these difficulties it will be necessary to develop substantially the regulatory accounting arrangements pertaining to companies owning electricity and gas networks that are subject to price control. As a first step consultants have been appointed to assist in developing revised cost attribution, allocation and inter-business charging guidelines for electricity distribution. Following detailed discussions with the companies a draft of the revised guidelines will be published for wider comment. In the light of this project and the experience of the present reviews of NGC's and Transco's price controls further cost guidelines will be developed covering each of the electricity transmission and gas transportation sectors.

2.8 At present price controls also apply to significant parts of each PES's electricity supply business and of Centrica's gas supply business. As competition develops in these markets the scope of the price controls is being reduced and so the existing price controls only apply to certain domestic customers. It is not practicable to use regulatory accounts, which apply to separate businesses or activities, rather than particular groups of customers, to monitor performance against the present supply price controls. Ofgem has more general powers to request information in order to monitor performance against these price controls and judge the development of competition. In time competition should be sufficiently well developed to make it possible to remove price controls entirely from supply businesses. This should provide an opportunity to remove the regulatory accounting arrangements pertaining to these businesses, although it will be necessary to consider whether this would create any inconsistencies with the provisions of the EU Directives on the internal markets for electricity and gas.

2.9 While there are no price controls applying to IPGTs Ofgem is required to approve the charging methods for these local gas distribution businesses. The regulation of IPGTs will be reviewed during 2001.

Detection of Anti-Competitive Behaviour

2.10 A number of the companies that presently prepare regulatory accounts also have licence obligations designed to prevent cross-subsidy between businesses, discrimination and other forms of anti-competitive behaviour. The requirements on licensees to produce regulatory accounts were originally designed to assist in the enforcement of these prohibitions.

2.11 Regulatory accounts are insufficient for the purpose of investigating anti-competitive behaviour in markets where competition is developing. This would require up to date information on how a company has arrived at a particular price and on wider aspects of a company's market behaviour and the flexibility to examine these matters over various time periods. In contrast regulatory accounts provide more aggregated data and relate only to fixed time periods.

2.12 Ofgem also has concurrent powers with the Director General of Fair Trading under the Competition Act 1998. The key provisions of the Competition Act 1998 came into force on 1 March 2000. It prohibits agreements which have the effect of preventing, restricting or distorting competition and prohibits the abuse of a dominant position in a market. This framework is designed to operate without the support of annual regulatory accounting information, although an investigation under the Competition Act 1998 may involve consideration of accounting data, including information derived from a company's management accounts and detailed information on costs, revenues and prices.

2.13 These factors suggest that the primary purpose of regulatory accounts should be to support the regulation of those monopoly businesses subject to on-going price control. Nevertheless, there will continue to be wider benefits than those associated with the price control. The preparation and adoption of agreed regulatory accounting guidelines would enhance Ofgem's understanding of the issues involved in the attribution and allocation of costs between activities and should provide additional reassurance that costs associated with other activities are not being hypothecated to network businesses.

Securing Financial Health

2.14 In the light of the large amount of corporate restructuring that has taken place since 1995 Ofgem has introduced financial ring-fencing provisions designed to safeguard the financial wellbeing of distribution and transmission businesses. These conditions, which are forward looking, provide a more effective approach to protecting the financial position of a business than monitoring regulatory accounts.

2.15 Nevertheless, if the quality and consistency of information in regulatory accounts is improved then they would provide useful information which may assist a variety of users to assess trends in the financial position of a regulated business. The requirements that monopoly businesses should be held in separate companies and the financial ring-fencing conditions should also allow the regulatory accounts to contain information on the financing of these businesses, including interest, dividends and tax.

Overview

2.16 At present in the gas industry regulatory accounts are prepared by BG Transco plc and Centrica (the successor companies to British Gas plc). In addition IPGTs are also required to prepare regulatory accounts. In the electricity industry regulatory accounts are prepared by the successor companies to the CEGB, the Area Boards and the Scottish Electricity Boards. The successor companies to the CEGB are National Grid Company plc, British Energy plc, BNFL plc (which owns the Magnox power stations that were originally owned by the CEGB), First Hydro Company (which now owns the pumped storage stations) PowerGen plc and National Power plc. The successor companies to the Area Boards were the Regional Electricity Companies and the successor companies to the Scottish Electricity Boards were Scottish Power and Scottish Hydro. New entrants in to electricity generation and electricity and gas supply and gas shipping have not been required to prepare regulatory accounts.

2.17 The discussion earlier in this chapter suggests that the requirements to prepare regulatory accounts should focus on companies subject to price control. This suggests removing the existing requirements on all electricity generation businesses and second tier electricity suppliers. As supply price controls are removed then requirements on all supply businesses to produce regulatory accounts could be removed. These possible new arrangements are summarised in table 2.

2.18 However, as noted in paragraph 1.5, it would be necessary to ensure that changes to licence conditions do not create inconsistencies with the EU Directives on the internal markets for electricity and gas. Therefore, where a requirement to produce regulatory accounts is to be removed, it may be necessary to consider how compliance with the relevant section of the Directive is achieved.

TABLE 2: POSSIBLE FUTURE REGULATORY ACCOUNTING ARRANGEMENTS

Regulatory Accounts Relating to Electricity Businesses	
Companies	***Businesses***
Regional Electricity Companies	Distribution Supply(1)
Scottish Power(2), Scottish Hydro(2)	Transmission Distribution Supply(1)
National Grid Company	Transmission(3)
Regulatory Accounts Relating to Gas Businesses	
Companies	***Businesses***
Centrica	Supply(1) Shipping(1)
BG Transco	Transportation(3)
IPGTs	Distribution(4)

(1) Requirements to be removed as price controls are removed.

(2) Consideration to be given to retaining the requirements to produce regulatory accounts for generation, interconnector and wholesale activities until arrangements for GB-wide trading are in place.

(3) Scope of the regulatory accounting arrangements to be reviewed following completion of the present price control reviews.

(4) Scope of the regulatory accounting arrangements to be reconsidered following the review of IPGT regulation in 2001.

2.19 Views are invited on any aspect of the issues raised in chapters 1 and 2 and in particular on the suggestions that:

- the timetable for this review should be as set out in paragraph 1.18;
- the main purpose of regulatory accounts should be to inform price control reviews and monitor company performance between reviews;
- the quality of information contained in the regulatory accounts of network businesses should be substantially improved;
- regulatory accounts are not the most effective way of dealing with anti-competitive behaviour (including price discrimination and cross-subsidy) or securing the financial wellbeing of a business; and
- the arrangements for regulatory accounts should be as summarised in table 2.

3 Regulatory Accounts and Price Controls

Introduction

3.1 There are four broad features of regulatory accounts that are important if they are to provide high quality information that can be reconciled with the assumptions underlying a network price control. First, there is an issue relating to the way in which different bases of accounting establish a value for assets. It is appropriate for assets to be valued in a way that is easily understood and facilitates comparisons with the assumptions underlying the price controls. Second, cost attributions and allocations and inter-business charging must be conducted on a transparent and reasonable basis. Third, the reporting period for the regulatory accounts should be consistent with the price control. Fourth, the regulatory accounts must be presented in a way that facilitates comparisons with the price control. This chapter deals with these issues in turn.

Basis of Preparation

3.2 At present regulatory accounts in the electricity industry are prepared on the basis of current cost accounting (CCA), following the practice of the industry before privatisation. BG Transco used CCA until 1997 when it was replaced by Modified Historical Cost Accounting (MHCA) for both regulatory and statutory purposes. The majority of companies in the UK use Historical Cost Accounting (HCA) as the basis of preparation for their statutory accounts.

3.3 In setting network price controls Ofgem uses regulatory asset values (RAVs) as the basis for allowances for depreciation and returns rather than CCA, HCA or MHCA asset values. Nevertheless, the financial modelling, which is used during the price control review to inform judgements about the financial viability of network businesses uses HCA principles, as this is broadly consistent with the approach adopted by credit rating agencies. The main options for valuing fixed assets (CCA, HCA, MHCA and RAVs) in the regulatory accounts are described in more detail below. As asset lives for network assets tend to be relatively long, the differences between current replacement costs and historical acquisition costs can be large. Although RAVs include an annual revaluation to take account of the effects of inflation they are generally below CCA values, although in the longer term there may be some convergence between these two methods.

3.4 Presently CCA is the basis used by the majority of companies preparing regulatory accounts. The most important difference between HCA and CCA lies in the treatment of fixed assets. Under CCA rules fixed assets are shown at their current replacement cost (less accumulated depreciation) unless their value is deemed to have been impaired, in which case they must be written down to their estimated recoverable amount, being the higher of value in use and net realisable value. To implement CCA rules a company will review on a regular basis the replacement values of its fixed assets. In many cases this includes an annual revaluation of those fixed assets. This can be a relatively subjective exercise and CCA information can be difficult to interpret.

3.5 Under HCA, fixed assets are shown in the balance sheet at their acquisition cost (less accumulated depreciation), unless their value is deemed to have been impaired, in which case they must be written down to their estimated recoverable amount, being the higher of value in use and net realisable value. HCA is used by the majority of companies in the UK and has the advantage that it is widely understood. It is also generally regarded as less subjective than CCA, although (as with any approach to asset valuation) it will be affected by capitalisation policy. In reviewing network price controls the financial modelling used to inform judgements about financial viability is also carried out on an HCA basis. Given these advantages there is clearly a strong case for prescribing an HCA basis for regulatory accounts in the future.

3.6 The introduction of Financial Reporting Standard 15, which is effective for accounting periods ending after 23 March 2000, has formalised the rules governing asset revaluations. Accounts that are prepared based on regular revaluations of fixed assets are referred to as being prepared on a MHCA basis. Revaluations of fixed assets can be made using replacement costs, provided this is not in excess of their estimated recoverable amount.

3.7 It has been suggested that MHCA principles are sufficiently flexible to allow the preparation of accounts on a basis consistent with that used by regulators in setting network price controls. However, at present it is not clear to what extent companies in general will move toward MHCA principles and so the case for HCA principles remains compelling.

3.8 In setting price controls Ofgem has adopted an approach to calculating RAVs that is based on rolling forward an initial privatisation or market valuation by adjusting for depreciation, fixed asset additions, disposals and inflation. The main differences between HCA and RAV relate to the value of fixed assets and the associated depreciation charge. This would mean that it would be relatively straightforward to provide a reconciliation from historical cost values to the RAVs by means of an additional note to the HCA accounts.

Guidelines for Cost Attribution, Allocation and Inter-Business Charges

3.9 Businesses typically incur some costs that can be attributed to specific activities and others that cannot be so attributed but are nevertheless legitimately associated with the business, such as certain corporate overheads. Also businesses may have contracts with external suppliers or other businesses within the same group. These cost structures necessitate principles to govern cost attribution, the allocation of legitimately incurred non-attributable costs and the basis of inter-business charging. In addition it is necessary to determine which costs should be treated as operating expenditure and which costs should be capitalised and added to the asset base.

The Present Position

3.10 Where they exist the present cost guidelines have remained virtually unchanged since their introduction at privatisation. This is unlike most of the other regulated industries, where regulators have typically issued detailed accounting guidelines.

3.11 For the PESs the guidelines presently in force are known as CSC 194. These were developed before privatisation and have remained largely unchanged since then. Recent experience and in particular the detailed work carried out in 1999 as part of the work on proposals for business separation and revised price controls has revealed that these guidelines are no longer appropriate. In particular they have allowed each PES too much flexibility in areas such as the attribution and allocation of costs, resulting in inconsistencies between companies and a tendency to hypothecate extra costs to distribution activities and businesses. For other parts of the electricity and gas industries no detailed guidelines exist. A more detailed description of the sort of difficulties that have arisen is set out below:

- general group expenses and corporate overheads, such as certain advertising and marketing, finance functions and costs associated with the group board, have typically been allocated to network businesses in a way that leads to an undue proportion of these costs being associated with monopoly activities;

- where a network business uses the same services as a competitive activity the costs of these services have tended to be inappropriately allocated. The last electricity distribution price control revealed that the existing costs allocation guidelines allowed costs to be allocated on the basis of somewhat arbitrary assumptions rather than attributed using appropriate cost drivers. For instance, CSC 194 allowed certain customer service costs to be allocated 50 per cent to distribution and 50 per cent to supply. In the price control review this allocation was replaced by an attribution based on the number of customer contacts relating to distribution and supply activities;

- certain groups are structured so that services used by a network business are provided by a service company within or affiliated to the wider group of companies of which the network business is a part. Typically the charge for the provision of the service includes an element of profit. An effect of these arrangements can be an increase in the costs of the network business and the transfer of profits to elsewhere in the group. In the distribution price control review these extra profits were removed from the cost base;

- during the last electricity distribution price control review it became apparent that a number of PESs had made changes to their capitalisation policies, which tended to reduce the level of their reported operating costs and increase capital expenditure. These changes related mainly to IT, metering and repairs and maintenance costs. As a consequence of this it was necessary to make significant adjustments to the accounting data provided by PESs. These were intended to prevent distortions in the calculation of regulatory asset values and so prevent PESs gaining in an inappropriate way from changes in accounting policies; and

- certain provisions and one-off costs have been treated differently in the regulatory accounts when compared to the approach adopted in resetting price controls.

3.12 For companies with network price controls financial ring-fencing and separation provisions have been or are in the process of being put in place. These require network businesses to be placed in separate companies, restrict the extent of unregulated activities and require services from elsewhere within the group to be provided on an arms length basis. These measures should reduce the need to allocate costs between businesses carried on in the same company. Nevertheless, important issues will remain relating to inter-business charges. These will be more pronounced in the future as companies are contracting out additional activities, to both affiliated and unrelated companies.

The Development of Revised Guidelines

3.13 There are a range of approaches that could be adopted in formulating guidelines. For instance the guidelines might contain detailed rules on the treatment of activities, costs and recharges. Another approach would be to specify a detailed framework of principles within which the licensee would be required to develop policies and procedures for its specific circumstances. These different approaches are discussed in more detail below. Whatever the form of the regulatory accounting guidelines they should lead to accounts that are consistent, objective and transparent. It is also important that the accounts can be reconciled in a reasonably straightforward way with the assumptions underlying the price control and the statutory accounts.

3.14 It would be possible to establish a set of detailed rules governing cost attributions, allocations, inter-business charges and capitalisation policy with which each licensee would be required to comply with in formulating its regulatory accounts. The aim of such rules would be to ensure regulatory accounting information suitable for price control purposes and to promote a high degree of consistency between licensees. However, such rules would need to be extensive to deal with the wide range of business structures and arrangements that companies have adopted. Devising and implementing these detailed rules would require substantial resources. Given the nature of cost allocation issues, these rules would have to be constantly reviewed to reflect changes in circumstances. Companies might also have an incentive to organise their affairs so that the rules distorted the underlying costs of the regulatory business, or have less incentive to reorganise businesses efficiently if the accounting rules did not work in a way favourable to the reorganisation. The on-going difficulties associated with detecting these problems and enforcing appropriate rules would be significant.

3.15 Establishing a detailed framework of principles would be a less prescriptive and more flexible approach than the detailed rules discussed above. An approach of this nature could be applied whatever business structure a licensee chooses to adopt. The October 1998 consultation paper described some of the principles that might be included in such a framework, for instance:

- all charges by affiliates or service companies to a network business should as far as practicable be based on costs that are directly attributable to the network business;
- any service unit must have adequate accounting systems for identifying such attributable costs at the level of individual activities;
- where charges include a mark-up on attributable costs this should be identified and disclosed in the regulatory accounts, and accompanied by a statement of the policy by which the mark-up is determined;
- where a licensee accepts charges of whatever nature from a service unit, the licensee should have full access to the service unit's financial and other records;
- these principles should apply equally to charges for all categories of cost including capital costs. Similar principles would also apply to any charges made by a regulated business to an affiliated business; and

- where the basis of any charged recognised in the regulatory accounts is inconsistent with an explicit assumption made in setting the price control this should be disclosed and explained.

3.16 While this approach would not secure standardisation in the detailed policies and practices adopted by differing licensees, it may secure as much comparability as is realistically possible given the different organisational structures of network businesses. Nevertheless, there may be certain areas or aspects of a network business where it might be appropriate to have more detailed rules, for instance in relation to capitalisation policy. These matters will be considered further in the light of the consultants work on the electricity distribution sector.

3.17 It would also be necessary to develop a suitable approach to enforcing these guidelines. Chapter 4 discusses issues relating to the audit of regulatory accounts. In addition Ofgem would need to develop procedures and processes for monitoring regulatory accounts, investigating difficulties and developing and enforcing suitable remedies.

Reporting Periods

3.18 At present certain electricity licence holders require Ofgem's consent before they can change the reporting period for their statutory and regulatory accounts. Consent to change reporting periods has been conditional on the licensee agreeing to provide information in its regulatory accounts consistent with a 31 March year end. This ensures that the information contained in the regulatory accounts relates to the same period across all companies and is consistent with the price controls.

3.19 In both the electricity and gas industries price controls are based on reporting periods ending 31 March and so having all regulatory accounts prepared with this year end would aid consistency and transparency. This would be a new requirement for gas companies.

Format of the Regulatory Accounts

3.20 The existing arrangements do not specify in detail the format for the regulatory accounts. This has led to a situation where the majority of companies present information in a way which is not straightforward to reconcile to the assumptions made in setting their price controls. Appendix 2 sets out a draft template for electricity distribution regulatory accounts which is designed to deal with some of these difficulties. It will be further developed in the light of responses to this paper, discussion with companies and the work of consultants on cost attribution and allocation guidelines.

3.21 Views are invited on any aspect of the issues raised in this chapter and in particular on:

- whether HCA principles with additional notes setting out each company's view of its regulatory asset value should be the basis for regulatory accounts;
- whether the approach to developing revised regulatory accounting guidelines should be as summarised in paragraphs 3.15 and 3.16 above;
- how any new arrangements should be monitored and enforced;
- whether the reporting period for all regulatory accounts should relate to the financial year ending 31 March; and
- the draft template for electricity distribution regulatory accounts set out in appendix 2.

4 Audit Arrangements

Introduction

4.1 Each licensee that is required to prepare regulatory accounts also has to arrange for these accounts to be audited. The provision of an audit report is an important part of the requirements for regulatory accounts as it should enhance the quality, objectivity and credibility of the accounts, both to the regulator and to other users. At present, the auditors of a licensee's statutory accounts typically audit its regulatory accounts. This, combined with the problems identified in previous chapters relating to the consistency and quality of information contained in regulatory accounts, raises a number of issues regarding the effectiveness of the existing audit arrangements for regulatory accounts.

4.2 The issues relating to audit arrangements set out in this chapter are being discussed with the Auditing Practices Board and the Institute of Chartered Accountants in England & Wales.

Appointment of Auditors

4.3 It is for consideration whether a company's statutory auditors should be allowed to perform the audit of its regulatory accounts. If the audit of the regulatory accounts were to be carried out on a basis independent of the statutory audit this might improve the objectivity and credibility of the regulatory accounts. It might also make it possible for the same firm to audit the regulatory accounts of all the companies in the energy sector so enhancing the consistency of regulatory accounting information across companies. However, appointing such auditors might increase the costs of the audit if the auditors of the regulatory accounts needed to duplicate some of the work associated with the statutory audit.

4.4 In the light of these possible extra costs it is necessary to consider whether other measures might be adopted that would nevertheless enhance the effectiveness of the existing arrangements. These might include modifying the existing licence conditions to provide Ofgem with the authority to:

- require the appointment of a different auditor if the existing audit arrangements prove unsatisfactory;

- require a second audit by the licensee's auditors;

- require a second audit by a different auditor; and

- require a second audit of specific areas of concern, perhaps with the same auditors reporting on a number of different companies.

4.5 It will be important to consider the costs and benefits of these various measures before making final proposals with respect to these matters. If the regulator is going to require the appointment of a particular firm of auditors it would also be necessary to consider whether they should be remunerated by Ofgem or the licensee.

Duty of Care, Materiality and the Audit Framework

4.6 At present the auditor's have a duty of care is to the regulated company. It is not clear whether the auditor's also have a duty of care to Ofgem. Given that Ofgem relies upon the audit report, the auditor should also owe a duty of care to Ofgem and so the existing arrangements need to be clarified.

4.7 At present the materiality level used for the audit of group level statutory accounts may also be used as the materiality level for the audit of the regulatory accounts. For some companies the group may be significantly larger than its regulated activities. In these circumstances the appropriate level for an issue to be material to the audit of the group may be significantly in excess of the appropriate materiality level for a regulated activity or business. Therefore, it may be more appropriate for Ofgem to either set or approve the materiality levels for the audit of the regulatory accounts. Transparency could also be improved by disclosing either in the audit opinion or on the face of each accounting statement the materiality level used in the audit.

4.8 It is necessary to consider how any regulatory accounting guidelines should relate to more general accounting standards. It may be appropriate for the regulatory accounting guidelines to take precedence over other accounting standards in the preparation of regulatory accounts. Where the regulatory accounting guidelines do not cover an issue then UK Generally Accepted Accounting Practice (UK GAAP) should be used. There may also be some issues that could be covered by developing a Statement of Recognised Practice (SORP) for regulated businesses in the electricity and gas industries, although a SORP cannot override more general accounting standards.

4.9 Although audit reports are addressed to the regulator, the wording of the audit opinion could be rationalised. If regulatory accounting guidelines are going to take precedence over other accounting standards in the preparation of regulatory accounts, then it may no longer be appropriate to use "true and fair view" in the audit opinion. Another option would be "presents fairly in accordance with" which may be a better form of wording for the audit opinion.

4.10 Some of the issues identified above might be dealt with in the engagement letters with auditors. The existing engagement letters deal with the relationship between the regulated company and the auditor. These could be modified to include Ofgem or there might be separate engagement letters between Ofgem and the auditor. The intention would be to place the relationships between all three parties on a more formal basis and could include:

- the duty of care owed by the auditor to Ofgem and liability levels;
- the disclosure of sensitive information to Ofgem;
- the process for holding tri-partite meetings and written communication between the auditor, regulated company and Ofgem and bi-lateral communications between the auditor and Ofgem; and
- materiality levels.

4.11 Views are invited on any aspect of the issues raised in this chapter and in particular on:

- whether a licensee's statutory auditors should be allowed to perform the regulatory accounts audit;
- whether there is merit in the same firm auditing the regulatory accounts of all the licensees in the electricity and gas industries;
- if the regulator is going to require the appointment of a particular firm of auditors whether they should be remunerated by Ofgem or the licensee;

- whether the auditors of the regulatory accounts should have a duty of care to Ofgem;
- the specification of materiality levels for the audit of regulatory accounts;
- whether the regulatory accounting guidelines should take precedence over other accounting standards in the preparation of regulatory accounts; and
- the appropriate form and content of engagement letters.

5 Other Matters

Publication issues

5.1 At privatisation most of the successor companies were listed companies that prepared and published statutory accounts consistent with London Stock Exchange requirements and UK GAAP. The activities of these companies were dominated by their regulated businesses and so their statutory accounts contained information on the performance of these businesses. Since privatisation many regulated businesses have become part of larger groups of companies, some of which are not listed. While they are still required to produce statutory accounts these contain less detailed information and are not widely available.

5.2 It would seem appropriate that in future all companies in the electricity and gas industries should be required to publish their regulatory accounts and make them available on the internet. It will be important that the published version of the regulatory accounts contains a full range of information. In future this will need to include a note setting out the licensee's estimate of its regulatory asset value, a full narrative section, a detailed statement of cost attributions, allocations and recharges and the additional information normally only required as part of a listed company's statutory accounts. The introduction of financial ring-fencing provisions and revised separation arrangements will also allow the regulatory accounts to include information on financial structure (tax, interest and dividends). In addition a reconciliation should be available between the information in the regulatory accounts and other relevant information, such as the statutory accounts or data on capital expenditure contained in quality of supply reports.

5.3 At present regulatory accounts are sent to Ofgem up to 6 months after the end of the year. The companies that presently produce regulatory accounts in the electricity and gas industries usually publish their statutory accounts substantially earlier. A more suitable timetable for the accounts to be published might be within 4 months of the financial year-end.

5.4 At the moment interim regulatory accounts are prepared on a half yearly basis by electricity and gas licensees. In general these interim accounts contain relatively little detailed information and add relatively little to the information contained in the annual regulatory accounts. In the light of these factors it may be appropriate to remove the requirements on all licensees to produce interim regulatory accounts

Provision of narrative

5.5 At present the published regulatory accounts lack a detailed commentary that would explain to users the figures included in them. This deficiency is due to the relevant licence conditions only requiring certain primary financial statements, their associated notes and the auditor's report to be included in the regulatory accounts.

5.6 The lack of an adequate descriptive analysis can be resolved by requiring the following to be included in the regulatory accounts:

- a commentary discussing the results (where appropriate this commentary should be structured as an operating and financial review);
- a comparison of actual results to the assumptions made in setting the price control;
- an explanation of the variances between the actual results, the results of the previous year and the assumptions made in setting the price control; and
- discussion of results against plan and an outline of the forward plans for key business drivers such as principal capital expenditure projects, financing arrangements, organisational shape, quality of supply improvements and so on.

5.7 Views are invited on any aspect of the issues raised in this chapter and in particular on:

- how regulatory accounts should be published;

- the level of detail that should be included on cost attributions and allocations;
- where a licence holder is not a separately listed company producing statutory accounts, whether the same type of information normally required as part of these accounts should be included in the published regulatory accounts;
- whether the published regulatory accounts should contain additional information such as that relating to capital structure and a reconciliation to the statutory accounts;
- the most suitable timetable for publication;
- whether interim regulatory accounts should be discontinued; and
- the requirements to include a detailed narrative with the regulatory accounts.

Appendix 1: Summary of the Responses to the 1998 Consultation Paper

1.1 OFFER received 32 responses to the October 1998 consultation paper on regulatory accounts. Responses were received from 14 PESs, 5 generators, 6 Electricity Consumer Committees (ECCs), 5 from other companies or groups representing companies in the electricity or gas industries and 2 other groups. A list of respondents is set out below.

Overview

1.2 The PESs agreed in principle to increased transparency for monopoly businesses, but said that the issues of business separation need to be resolved before deciding future regulatory reporting requirements. The ECCs supported the provision of additional information and said that the regulatory accounts should be published in full. There was widespread support for the development of a framework of principles incorporated into the licence for cost attribution, allocation and inter-business charging.

Summary of Responses by Group

PESs

1.3 The majority of PESs supported increased transparency in the regulatory accounts for monopoly businesses, provided an appropriate balance could be maintained between achieving this and not overburdening businesses with requirements to publish unnecessary detail. They also said issues relating to business separation need to be resolved before deciding the future scope of the regulatory accounts.

1.4 For competitive businesses such as generation and supply the PESs suggested that regulatory accounting requirements could be reduced or removed. The Scottish PESs recommended abolishing the existing requirements to account separately for their wholesaling and interconnector businesses.

1.5 Where specifically mentioned, there was support for a number of proposed changes, namely the inclusion of a narrative that covers the broad trends of expenditure and cost performance from year to year. However, the majority of PESs disagreed with the concept of publishing forecast information, as this would take reporting well beyond normal accounting requirements.

1.6 Several PESs supported a more detailed and relevant classification of costs. Other PESs said that differences in organisational structures are likely to invalidate detailed inter-company comparisons. Another PES suggested that the regulatory accounts should separate controllable costs from other costs (e.g. exit charges, depreciation and network rates). There was general support for the development of a framework of principles approach to cost allocation and charging, rather than a detailed set of rules which would be inflexible and inappropriate.

1.7 Six PESs agreed that it would be reasonable to produce the regulatory accounts within three months of the financial year end. Others were unclear of the benefits of this or were concerned about the additional cost.

1.8 A number of PESs supported CCA as the basis for regulatory accounts while others HCA. There was some agreement that it would be helpful to disclose regulatory asset values.

Generators

1.9 In general generators linked the requirement to produce regulatory accounts with the degree of competition in a separated business. A number of generators suggested removing the requirements on businesses in the generation sector to produce regulatory accounts.

1.10 The generators tended to support the development of a framework of principles for cost attributions, allocations and inter-business charging. All the generators supported the production of the regulatory accounts on an HCA basis. There was also support for the disclosure of the regulatory asset values.

ECCs

1.11 The ECCs suggested that regulatory accounts should be published in full. There was also support for all the additional information requirements, particularly, the publication of an explanatory narrative, the cost attribution and allocation statements and a reconciliation between statutory and regulatory accounts. All the ECCs supported publication within 3 months of the financial year end.

1.12 Some of the ECCs suggested that regulatory accounting arrangements should continue to apply to supply businesses and in certain circumstances second tier supply businesses.

1.13 All the ECCs wanted comparable and consistent information on costs. Some said this should be achieved by defining appropriate cost classifications. In particular, the regulator should issue an unambiguous list of monopoly business functions (with definitions) for which costs must be reported separately. Such functions need to be sufficiently disaggregated to highlight the relative importance of different activities, particularly those not resourced entirely from within the monopoly business. Others preferred adopting a framework of appropriate principles to deal with issues relating to cost attribution and allocation.

1.14 Several ECCs suggested that the regulator should publish inter-company comparisons based on regulatory accounting data, including a commentary on the relative significance of the various cost ratios and their relation to the assumptions used in setting price controls.

1.15 One ECC suggested the regulator should appoint the auditors and cited the OFWAT arrangements for audit verification, covering such things as pricing investigations and submitted business plans.

Other Companies in the Electricity and Gas Industries

1.16 Other industry respondents suggested that if the regulatory accounts are going to be of use to customers, they need to be able to understand the underlying cost and revenue drivers. Broader information on classes of costs and on cost attribution, allocation and inter-business charging, would be a key factor in achieving this understanding. OFFER should focus on ensuring that the regulatory accounts allow price controls to be tracked for the following key measures: operating expenditure, capital expenditure, asset value and return on assets.

Other

1.17 Other respondents generally supported the publication of a full set of information relating to regulatory accounts. They also stressed the importance of developing a co-ordinated policy on financial reporting across the various industries and sectors subject to regulation.

LIST OF RESPONDENTS

Eastern Group
East Midlands Electricity
London Electricity
Midlands
Northern Electric
NORWEB
SEEBOARD
Southern Electric
SWALEC
South Western Electricity
Yorkshire Electricity
Scottish Hydro-Electric
ScottishPower/Manweb

BNFL
British Energy
First Hydro
National Power
Powergen

ECC Chairmen's Group
East Midlands ECC
Merseyside and North Wales ECC
North East ECC
North West ECC
South West ECC

Association of Electricity Producers
BG plc
British Gas Trading
Enron Europe Ltd
National Grid Company

Consumers' Association
National Consumer Council

Appendix 2: Draft Template for the Regulatory Accounts

Introduction

2.1 This appendix sets out a draft template for the regulatory accounts of an electricity distribution business. It will be important that the format facilitates reasonably straightforward comparisons across time and between companies, with the assumptions underlying the price control and with the statutory accounts.

2.2 The draft template includes a significant amount of information. In finalising the template it may be necessary to aggregate certain categories of information. For instance it may not be reasonable to try and split information in the balance sheet between activities. The level of detail shown in the analysis of operating costs is greater than Ofgem collected in the last price control review, so in comparing actuals to the price control it would be necessary to aggregate some of the items in the analysis of operating costs. Also the definition of distribution activities will require further consideration.

2.3 Over the years since privatisation there have been a number of structural changes to the organisation of PES distribution businesses. Certain activities are now outsourced to related group companies. It is likely that there will be further developments of this sort. As a result of all these changes and other factors it may be necessary to supplement the traditional analysis of costs by inputs with more functional or activity based analysis.

2.4 An example of the problems these issues might cause could be the cost of an IT help desk. A company could perform this function in-house in which case there would be employment costs and office costs or the function could be outsourced in which case there would be an external recharge. In a comparison between two distribution businesses where one company uses the in-house option and the other outsources then employment costs, office costs and other external costs may no longer be directly comparable. However, they may be comparable at a functional or activity level.

2.5 The main activities within a distribution business might include:

- Network operation (encompassing repairs and maintenance, network control, planning and asset management, MPAS)
- Metering
- Connections
- Excluded services
- De-minimis activities

2.6 Generally, the tables in the template are consistent with UK GAAP for a listed company, but certain tables would require the provision of additional information. In particular it will be important to be able to compare the actual costs of running the company with the assumptions underlying the price control and gain a better understanding of any variances.

2.7 The additional tables that have been included are:

- executive Summary ;
- some parts of the review of the year are additional;
- analysis of turnover;
- analysis of operating costs;
- analysis of the source of operating costs;
- analysis of non-exceptional one-off costs;
- analysis of capital expenditure; and
- detailed statement of the principles involved in cost allocation and capitalisation.

2.8 The tables should be read in conjunction with the following notes:

- information that is not provided either in the regulatory accounts or on the additional electronic return, is marked with a hash sign;
- some of the operating costs could be broken down into more detail e.g. employment costs could be broken down into salary, national insurance and pension costs (this information is currently provided in the electronic return);
- provisions will be analysed in a separate note in the notes to the accounts;
- all tables will include a comparison with the prior year;
- the extent that information will be required by activity is for consideration; and
- throughout the tables actuals will be compared to price control assumptions.

The Template

Contents List

1. Executive Summary
2. Review of the year
3. Profit and loss account
4. Statements of total recognised gains and losses
5. Balance sheet
6. Cash flow statement
7. Analysis of turnover
8. Analysis of operating costs
9. Analysis of the source of operating costs
10. Analysis of capital expenditure

11. Analysis of non-exceptional one-off costs
12. RAV statement
13. Chairman's statement
14. Director's report
15. Corporate governance
16. Directors remuneration
17. Auditors report
18. Accounting policies (including detailed statement of the principles involved in cost allocation and capitalisation)
19. Notes to the accounts (includes the provisions note – see table 13 for the template)
20. Five year summary

1 Executive Summary

Commentary

Key Statistics **Separate business**	**Actual (A)** **00/01** **£m**	**Actual (B)** **99/00** **£m**	**Price control (C) #** **00/01** **£m**	**Var (A-C)** **00/01** **£m**
Profitability				
Turnover				
Profit before tax				
Return on RAV #				
Earnings per share #				
Dividends				
Other key statistics				
Capital expenditure				
Disposals of fixed assets				
RAV #				
Net assets				
Net debt				
Staff in post				
Gearing				
Interest Cover				
Dividend Cover				

2 Review of the year

Introduction

The aim of the review of the year is to give users of the accounts a better understanding of the company's position, performance and future prospects. It will also allow key issues to be identified e.g. risks to the business.

Typical contents would be:

Operational

- Key factors affecting business
- Management of risks
- Projects
- Use of resources
- People
- Environment
- Health and safety

Financial

- Capital structure
- Treasury
- Use of cash resources
- Liquidity

Comparison to the price control

- Operating costs
- Capital expenditure
- Operational performance

Prospects for following year

- Cost reduction programmes
- Capital expenditure programmes
- Financing requirements
- Organisation of manpower

3 Profit and Loss Account

Profit and Loss Account **For the year ended xx xxxxx xxxx** **Separate business**	**Actual** **(A)** **00/01** **£m**	**Actual** **(B)** **99/00** **£m**	**Price control** **(C) #** **00/01** **£m**	**Var** **(A-C)** **00/01** **£m**
Turnover				
- continuing operations				
- discontinued operations				
Total turnover				
Operating costs				
- continuing operations				
- discontinued operations				
Total operating costs				
Operating profit				
- continuing operations				
- discontinued operations				
Total operating profit				
Profit/(loss) on disposal of tangible fixed assets				
- continuing operations				
- discontinued operations				
Total profit/(loss) on disposal of tangible fixed assets				
Profit/(loss) on ordinary activities				
Net interest				
Profit/(loss) on ordinary activities before taxation				
Tax on profit on ordinary activities				
Profit/(loss) for the financial year				
Dividends				
Retained Profit/(loss) for the year				

Commentary

4 Statement of total recognised gains and losses

Statement of total recognised gains and losses For the year ended xx xxxxx xxxx Separate business	Actual (A) 00/01 £m	Actual (B) 99/00 £m	Price control (C) 00/01 £m	Var (A-C) 00/01 £m
Profit for the financial year				
Gains and losses				
Total recognised gains and losses for the year				

Commentary

5 Balance Sheet

Balance Sheet As at xx xxxxx xxxx Separate business	Actual (A) 00/01 £m	Actual (B) 99/00 £m	Price control (C) # 00/01 £m	Var (A-C) 00/01 £m
Fixed assets				
Tangible assets				
Investments				
Current assets				
Stocks				
Debtors				
Cash and deposits				
Creditors: amounts falling due within one year				
Borrowings				
Over-recovery of price controlled income				
Other creditors				
Net current assets/(liabilities)				
Total assets less current liabilities				
Creditors: amounts falling due				
due after more than one year				
Borrowings				
Other creditors				
Provisions for liabilities and charges				
Net assets				
Capital and reserves				
Called-up share capital				
Share premium account				
Capital reserve				
Capital redemption reserve				
Revaluation reserve				
Profit and loss account				

Commentary

6 Cash Flow Statement

Cash Flow Statements As at xx xxxxx xxxx Separate business	Actual (A) 00/01 £m	Actual (B) 99/00 £m	Price control (C) # 00/01 £m	Var (A-C) 00/01 £m
Net cash inflow from operating activities				
Investments and servicing of finance				
Interest received				
Interest paid				
Dividends received				
Dividends paid				
Taxation				
UK corporation tax paid				
Investing activities				
Payments for tangible fixed assets				
Payments for fixed asset investments				
Receipts from sales of tangible fixed assets				
Net (increase)/decrease in short-term deposits				
Net cash inflow/(outflow) before financing				
Financing				
Issue of ordinary shares				
Repurchase of ordinary shares				
New long term loans				
Repayment of loans				
Capital element of finance lease rentals				
Increase/(decrease) in net cash balances				

Commentary

7 Analysis of turnover

Analysis of turnover For the year ended xx xxxxx xxxx Separate business	Actual (A) 00/01 £m	Actual (B) 99/00 £m	Price control (C) # 00/01 £m	Var (A-C) 00/01 £m
Price controlled revenue				
Network				
Metering				
Other				
Total price controlled revenue				
Excluded services turnover				
NTR				
Pre-payment meters				
EHV charges				
Other				
Total excluded services turnover				
NGC exit charges				
De-minimis revenue				
Total turnover				

Commentary

8 Analysis of operating costs for the year ended xx xxxxx xxxx

Analysis of operating costs For the year ended xx xxxxx xxxx Separate business	Activity 1 00/01 £m			Activity 2 00/01 £m			Total 00/01 £m		
(Note: each activity is split between, A = Actual,	A	P	V	A	P	V	A	P	V
P = Price control and V = Variance).									
By type:									
Cost of sales									
NGC exit charges									
NTR costs									
Total cost of sales									
Other operating costs									
Controllable costs									
Staff costs									
Employment costs									
Redundancy and severance									
Temporary staff									
Consultancy									
Training									
Customer related									
Advertising and marketing									
Customer services									
Bad debts									
Office costs									
IT costs									
Professional fees									
Other office costs									
Other costs									
Health and safety									
Insurance									
Other									
Less controllable costs									
Rates									
Wayleaves									
Depreciation									
Total other operating costs									
Total operating costs									

Commentary

9 Analysis of the source of operating costs for the year ended xx xxxxx xxxx

Analysis of the source of operating costs For the year ended xx xxxxx xxxx Separate business	Direct 00/01 £m			Recharged 00/01 £m			Allocated 00/01 £m			Total 00/01 £m		
(Note: each activity is split between, A =	A	P	V	A	P	V	A	P	V	A	P	V
P = Price control and V = Variance).												
By type:												
Cost of sales												
NGC exit charges												
NTR costs												
Total cost of sales												
Other operating costs												
Controllable costs												
Staff costs												
Employment costs												
Redundancy and severance												
Temporary staff												
Consultancy												
Training												
Customer related												
Advertising and marketing												
Customer services												
Bad debts												
Office costs												
IT costs												
Professional fees												
Other office costs												
Other costs												
Health and safety												
Insurance												
Other												
Less controllable costs												
Rates												
Wayleaves												
Depreciation												
Total other operating costs												
Total operating costs												

Commentary

10 Analysis of capital expenditure for the year ended xx xxxxx xxxx

Analysis of capital expenditure **For the year ended xx xxxxx xxxx** **Separate business**	**Activity 1 00/01** **£m**			**Activity 2 00/01** **£m**			**Total 00/01** **£m**		
(Note: each activity is split between, A = Actual,	**A**	**P**	**V**	**A**	**P**	**V**	**A**	**P**	**V**
P = Price control and V = Variance).									
By type:									
Load related expenditure									
New business expenditure									
Industrial supplies									
New housing									
Substations and mains									
Services									
Meters									
Other									
Total new business expenditure									
Reinforcements									
Generation									
Removal of under-utilised assets									
Other									
Total load related expenditure									
Capital contributions									
Net load related expenditure									
Non load related expenditure									
Replacement expenditure									
Transformers									
Switchgear									
Sub-station other									
Overhead lines									
Underground cables									
Services									
Other									
Total replacement expenditure									
Meters									
Tele-control/SCADA									
Diversions									
Other									
Total non load related expenditure									
Total capital expenditure									

Commentary

11 Analysis of non-exceptional one-off costs

Analysis of non-exceptional one-off costs For the year ended xx xxxxx xxxx Separate business	Activity 1 00/01 £m			Activity 2 00/01 £m			Total 00/01 £m		
(Note: each activity is split between, A = Actual,	**A**	**P**	**V**	**A**	**P**	**V**	**A**	**P**	**V**
P = Price control and V = Variance).									
By type:									
One-off cost 1									
One-off cost 2									
Other non-exceptional one-off costs									
Total non-exceptional one-off costs									

Commentary

12 RAV Statement

RAV Statement For the year ended xx xxxxx xxxx Separate business	Actual (A) 00/01 £m	Actual (B) 99/00 £m	Price control (C) 00/01 £m	Var (A-C) 00/01 £m
Actuals (nominal prices)				
Additions				
Disposals				
Real opening balance				
Real regulatory depreciation				
Real Additions				
Real Disposals				
Real closing balance				
Regulatory values (nominal prices)				
Opening balance				
Regulatory depreciation				
Closing Balance				
Inflation Adjustment Index				

Note: the format of this statement may need to be developed further.

Commentary

13 Analysis of provisions

Analysis of provisions For the year ended xx xxxxx xxxx Separate business	Activity 1 00/01 £m			Activity 2 00/01 £m			Total 00/01 £m		
(Note: each activity is split between, A = Actual,	A	P	V	A	P	V	A	P	V
P = Price control and V = Variance).									
By provision:									
Provision 1									
Opening balance									
Charge to profit and loss account									
Credited to profit and loss account									
Provisions utilised									
Closing balance									
Provision 2									
Opening balance									
Charge to profit and loss account									
Credited to profit and loss account									
Provisions utilised									
Closing balance									
Total									
Opening balance									
Charge to profit and loss account									
Credited to profit and loss account									
Provisions utilised									
Closing balance									

Commentary