

Office of Gas and Electricity Markets

Resource Accounts 2006-07

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(For the year ended 31 March 2007)

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Annual Report

Introduction

These Resource Accounts have been prepared and published by the Office of Gas and Electricity Markets (Ofgem). The Accounts have been prepared under a direction issued by HM Treasury in accordance with section 5(2) of the Government Resources and Accounts Act 2000. The Accounts demonstrate the resources that have been used to deliver Ofgem's objectives. These Resource Accounts have been prepared in accordance with the guidance set out in the Government Financial Reporting Manual.

Nature of Ofgem's Business and its Aim, Objectives and Activities

This document contains the Accounts of Ofgem for the year 1 April 2006 to 31 March 2007. It should be read in conjunction with the Ofgem Annual Report for 2006-07, which is published separately and available from Ofgem's website (www.ofgem.gov.uk).

Ofgem is a non-ministerial government department. In the parts of the gas and electricity markets where competition is established and effective, Ofgem withdraws from direct price regulation and increasingly relies on competition powers to regulate companies' behaviour and protect domestic and commercial consumers' interests. Where competition is not possible or sufficiently well developed, Ofgem protects consumers' interests by direct regulation, for example by regulating the charges of monopoly companies that run the national transmission and local distribution networks in England, Scotland and Wales.

Ofgem is governed by the Gas and Electricity Markets Authority. The Authority's responsibilities are set out in the Gas Act 1986, the Electricity Act 1989, as amended by the Utilities Act 2000, the Energy Act 2004 and related legislation.

In fulfilling its obligations Ofgem works closely with the Department of Trade and Industry (DTI), the Department for Environment, Food and Rural Affairs (DEFRA) and energywatch. Energywatch is the independent watchdog set up to protect and promote the interests of gas and electricity consumers.

Aim

Ofgem's primary objectives, duties and functions are set out in statute. From these, Ofgem has distilled its aim as follows:

To protect consumers' interests, wherever possible by promoting effective competition and only where necessary through regulation.

This means working on behalf of consumers to secure gas and electricity supplies which are competitively priced, reliable and safe. In particular, the Corporate Strategy 2006-2011 identified seven themes:

1. Creating and sustaining competition,
2. Regulating networks effectively,
3. Helping protect the security of Britain's energy supplies,
4. A leading voice in Europe,
5. Helping to protect the environment,
6. Helping to tackle fuel poverty, and
7. Better regulation

The Gas and Electricity Markets Authority

The Authority comprises executive and non-executive members. The Authority is the ultimate decision making body for all matters dealt with by Ofgem, setting overall strategy, policy and deciding major issues.

Basis of appointment

The Chairman of the Authority, Sir John Mogg KCMG, was appointed non-executive Chairman on 1 October 2003 for a period of five years by the Secretary of State for Trade and Industry following open competition. Prior to taking up his role, he was initially appointed as a non-executive member of the Authority from May 2003. The seven non-executive members of the Authority are also appointed by the Secretary of State in consultation with the Chairman of the Authority.

Alistair Buchanan was appointed Chief Executive and an executive member of the Authority on 1 October 2003. The appointment was made following open competition and the process was overseen by a Civil Service Commissioner.

The appointment of the other executive members of the Authority is undertaken in accordance with the Civil Service Management Code and the three Ofgem Managing Directors are members of the Authority so long as they hold these posts.

Details of the remunerations paid to Authority members can be found in the Remuneration Report.

Executive Members of the Authority who served during the year

Alistair Buchanan, Chief Executive, appointed in October 2003.

David Gray, Managing Director, Networks, appointed in May 2003.

Sarah Harrison, Managing Director, Corporate Affairs, appointed in May 2005.

Steve Smith, Managing Director, Markets, appointed in May 2004.

Non-Executive Members of the Authority who served during the year

Sir John Mogg joined the Authority as a non-executive member in May 2003 and was appointed Chairman in October 2003. His current appointment ends in September 2008.

Dr Robin Bidwell joined the Authority as a non-executive member in February 2003. His current appointment ends in February 2008.

Miriam Greenwood joined the Authority as a non-executive member in May 2004. Her current appointment ends in May 2007.

Judith Hanratty joined the Authority as a non-executive member in January 2005. Her current appointment ends in December 2007.

Jayne Scott joined the Authority as a non-executive member in May 2004. Her current appointment ends in May 2007.

Sir Keith Stuart joined the Authority as a non-executive member in December 2000. His final term ended in December 2006.

Professor Leonard Waverman joined the Authority as a non-executive member in May 2002. His current appointment ends in May 2007.

John Wybrew joined the Authority as a non-executive member in May 2004. His current appointment ends in May 2007.

Professor George Yarrow joined the Authority as a non-executive member in December 2006. His current appointment ends in December 2009.

The non-executive members are considered to be independent of management and comprise a majority of the Authority. Apart from the following issues in respect of shareholdings and their treatment, there were no company directorships or other significant interests held by Authority members which could give rise to a conflict with their responsibilities as members of the Authority.

Judith Hanratty holds options for shares in BP plc, her former employer. A close family member of John Wybrew holds shares in Shell and BP. Both have undertaken that they will not deal in these shares during the period in which they are members of the Authority and for a period of 12 months thereafter.

Attendance by the Chairman and the Non-Executives

Attendance during the year was as follows:

	<u>The Authority</u>	<u>Audit Committee</u>	<u>Remuneration Committee</u>	<u>Sustainable Development Committee</u>
Sir John Mogg	12/12	-	2/2	-
Dr Robin Bidwell	12/12	1/1	-	3/3
Miriam Greenwood	12/12	-	-	-
Judith Hanratty	11/12	1/2	-	2/3
Jayne Scott	12/12	4/4	2/2	-
Sir Keith Stuart	9/ 9	2/2	2/2	-
Professor Leonard Waverman	10/12	-	-	-
John Wybrew	11/12	2/4	-	3/3
Professor George Yarrow	4/4	-	-	1/1

The Chairman has continued to contribute extensively to the development of EU regulatory policy for energy in his role as Chair of the Council of European Energy Regulators (CEER) and European Group for Electricity and Gas (ERGEG). In addition, the Chairman and Non-Executives have played a full part in Authority business through their attendance and contributions at meetings of Committees of the Authority; Ofgem Seminars; briefing sessions; meetings with external stakeholders; visits; an open session to which the public were invited and in their contacts with Ofgem teams dealing with the areas of special responsibility assigned to them. In addition to the Audit and Remuneration Committees, members of the Authority have worked on sustainable development policy, and price control proposals in respect of transmission and distribution. There has been a working group on offtake policy. The Authority held an "Awayday" meeting in March 2007, in part in closed session involving the Chairman and non-executives, to consider a survey of its performance during the year, and a range of related topics on governance and procedures, designed to improve its efficiency and effectiveness.

Senior Management Team

The Senior Management Team (SMT) comprises all the executive members shown in the Remuneration Report. Its role is to assist the Chief Executive in the day-to-day running of the business. It meets weekly and decides, subject to the overall direction and control of the Authority, on all matters relating to management and resources.

Governance

The Authority has introduced a corporate structure with committees that have clear terms of reference. They provide the necessary structure to ensure that there is a strong framework of internal control throughout the organisation. During the year the Authority has fully reviewed its rules and procedures in respect of delegated powers with minor amendments and updating. The following paragraphs set out Ofgem's response to HM Treasury's Corporate Governance Code for Central Government Departments.

Audit Committee

From December 2006 the Audit Committee has been chaired by Jayne Scott. In December 2006 the non-executive member, Judith Hanratty was appointed to the Audit Committee. Sir Keith Stuart, previously chairman of the Audit Committee and Dr Robin Bidwell, member, left the Audit Committee. John Wybrew was re-appointed for a further year. The Chief Executive, Chief Operating Officer and other staff, the external auditors (National Audit Office) and the internal auditors (Chiene and Tait) attend by invitation.

The Committee's role is to advise the Accounting Officer and the Authority on all matters affecting the financial health, probity, external reputation or wider internal controls of the organisation. The Committee also oversees Ofgem's RPI-X cost control regime. The Committee met four times during 2006-07, including a workshop which facilitated discussion and review of a number of topics including risk management and HM Treasury's new Audit Committee Handbook.

Sustainable Development Committee

The Energy Act 2004 added a duty for Ofgem "to carry out its functions in the manner best calculated to contribute to the achievement of sustainable development". The Authority's Committee on Sustainable Development, Chaired by Dr Robin Bidwell, has continued its work of advising the Authority on a wide range of issues, and has also prepared a detailed report on Ofgem's sustainable development policies, priorities and activities. The 2006 report addressed Ofgem's work relevant to this theme including its contributions to managing the transition to a low carbon economy; eradicating fuel poverty and protecting vulnerable customers; promoting energy saving; ensuring secure and reliable gas and electricity supplies; and in supporting environmental performance.

Enforcement Committees

Under the Rules of Procedure, the Authority in 2003 created two types of Enforcement Committee. One can be called to consider enforcement action in relation to licence breaches, and the second considers compliance with the Competition Act 1998. The Enforcement Committees comprise Authority members, with a majority of non-executive members and a non-executive chairman.

Remuneration Committee

The Committee's role relates to the pay and performance of senior Ofgem staff, and succession planning. Full details of the Committee's membership, role and senior staff salary and pension entitlements are given in the Remuneration Report on pages 13 to 16.

Auditors

The Comptroller and Auditor General, who has been appointed under statute and reports to Parliament, has audited the Resource Accounts. The notional cost of providing audit services was £44,000. There was no auditor remuneration (actual or notional) for non-audit work.

The Committee of Public Accounts, following the publication of the C&AG's report 'Ofgem: Sale of Gas Networks by National Grid' in February 2006, took evidence from Ofgem on: its approval of the gas networks sale by National Grid; the approach to setting prices for the gas networks; and its role in overseeing the infrastructure of the gas networks. The Committee's report was published in November 2006.

The Accounting Officer has taken all the steps that he ought to have taken to make himself aware of any relevant audit information and to establish that Ofgem's auditors are aware of that information. So far as he is aware, there is no relevant audit information of which Ofgem's auditors are unaware.

Ofgem's internal audit service provides an independent appraisal service for management by measuring and evaluating the adequacy, reliability and effectiveness of management and financial control systems. Internal audit make recommendations based on the appraisal of each system reviewed. An annual assurance report is provided to the Accounting Officer. Ofgem have chosen to outsource the provision of the internal audit service to ensure wholly independent and fully professional analysis and recommendations. Our current provider is Chiene and Tait, who were first appointed on 1 April 2003 and subsequently reappointed following a competitive process for another term commencing 1 July 2007.

Sustainability Report

Taking account of the environment in Ofgem's work

One of Ofgem's main themes is to help protect the environment with an overall goal to assist the gas and electricity markets and industry to achieve environmental improvement as efficiently as possible. Ofgem has had secondary duties in relation to the environment and certain groups of consumers (future as well as present) for some time and Parliament, by way of the Energy Act 2004, has expanded Ofgem's secondary duties on sustainable development. Ofgem is committed to sustainable development and our economic, social and environmental duties put sustainability at the centre of Ofgem's work. Although other government departments have the biggest role to play in sustainability Ofgem will use its legal powers and independent voice to make a difference.

Ofgem also administers a number of the schemes and arrangements established by the Government under its Climate Change Programme. The main schemes are the Renewables Obligation (RO), which creates obligations for electricity suppliers, and the Energy Efficiency Commitment (EEC), which creates obligations for both gas and electricity suppliers. Ofgem also administers the Renewable Energy Guarantees of Origin arrangements and exemptions from the Climate Change Levy for renewables and CHP generators.

Ofgem has extensive knowledge of the environmental programmes based on our experience of their administration. Building on this, Ofgem will work with the DTI and the Devolved Administrations on changes to the RO, the RO Scotland, and the Northern Ireland RO, including measures to allow small generators easier access to RO Certificates. Ofgem will continue to work with Government on the next phase of the EEC. Ofgem will also amend the administrative processes and IT systems to reflect the outcomes of the current reviews of the RO and the EEC.

On 1 November 2006 Ofgem published its first Sustainable Development Report. The report reflects Ofgem's commitment to promote sustainable development and is structured around a set of five themes and fourteen indicators which have been developed to assess progress towards making the gas and electricity markets more sustainable.

Environmental Policy Statement (Internal Ofgem Operations)

In February 2002 Ofgem gained certification to ISO14001 standard for its internal operations' activities and has since retained the standard annually.

The policy refers to Operations matters and does not extend to Ofgem's statutory regulatory functions and duties. As part of this process Ofgem has set up an internal Environment Team that is responsible for defining and reviewing the environmental impacts, including objectives and targets that are either applicable to, or set for, the Ofgem Estate. The team is responsible for ensuring that the environmental targets set in respect of the ISO14001 standard are met.

Ofgem will conduct its operations in a manner that reflects best environmental practice and follow the established environmental management system to ensure continual improvement.

Ofgem is committed to:

- Adopting best practice in respect of all environmental requirements and agreements,
- Reviewing its operations to identify any adverse environmental impacts,
- Reducing office energy and resource consumption by the promotion of effective and efficient reduction methods, and by other means as appropriate, that are consistent with best practice, and
- Working with its suppliers and contractors in order to ensure that goods and services procured support its environmental policy.

Ofgem switched electricity supplier from 1 April 2007. 100 per cent of Ofgem's externally supplied electricity is now generated from renewable sources. A 'binless office' is also being planned which will increase the amount of recycling and reduce waste collection.

Ofgem has also implemented many other environmental and energy saving initiatives, for example:

- In 2003, a CHP unit was installed, so far saving in excess of 948 tonnes of carbon dioxide,
- Replacing four boilers has provided a 35 per cent improvement in domestic heating efficiency,
- LED lights are now used in communal areas and sensors have been installed to automatically switch off all non-emergency lighting in unoccupied office areas,
- Timers have been fitted to all kitchen water boilers and chilled water machines,
- Hot drinks machines using non-recyclable sachets have been withdrawn, and
- A recycling scheme for old mobile phones has been set up.

Suppliers

Environmental Procurement

The evaluation criteria for all procurements undertaken by the Procurement Team are based on best value for money, with the contract awarded to the most economically advantageous tender. However, where contracts have possible implications on areas covered by Ofgem's environmental policy such as catering, cleaning or other building type services, additional criteria based on Ofgem's own ISO14001 policies and suitability of the tenderer's own environmental policy will be included.

Creditor Payment, Policy and Performance

Ofgem is signed up to the Better Payment Practice Code. The Code is laid down by the Better Payment Practice Group, a cooperative forum of representatives of the business community and Government that seeks to help to improve the payment culture in the UK. In line with the code, Ofgem's standard terms and conditions for the supply of goods or services specify payment within 30 days, or other agreed credit terms, of receipt of goods or services or valid invoice, whichever is the later. During 2006-07 Ofgem paid 99 per cent of undisputed bills within these deadlines.

Employees

Training and Development

Ofgem's most important investment is in its people. An active policy of recruiting and retaining high calibre staff will also continue. Knowledge management software and processes will be further developed to give staff immediate access to the quality of information they need to work effectively.

During the year, Ofgem continued to give a high priority to training and developing all staff to enhance their professionalism in pursuit of Ofgem's objectives. To this end, Ofgem has developed a Learning and Development strategy, an element of which is a training plan setting out the themes that link training and development activity across the organisation to meet Ofgem's wide ranging goals and priorities.

This commitment is reflected in expenditure: £0.501 million was spent on training during 2006-07.

Employee Involvement

Ofgem attaches great importance to managing, developing and training its staff in accordance with best practice and has a Staff Consultative Committee.

Health and Safety

Ofgem recognises and accepts its legal responsibility in relation to the health, safety and welfare of its employees and for all other people using its premises or engaged on its activities. Ofgem will comply with the Health and Safety at Work Act 1974 and all other relevant legislation as appropriate. Ofgem is committed to the positive promotion of accident prevention and the elimination of incidents involving personal injury, illness or damage.

The Health and Safety policy statement describes Ofgem's responsibilities and objectives and is available to all employees.

Pension Liabilities

The main pension scheme for employees is the Principal Civil Service Pension Scheme (PCSPS). The pension liabilities arising from Ofgem's employees' membership of the PCSPS are not provided for in these accounts in accordance with HM Treasury's instructions, and are described in the Remuneration Report and Notes 1.8 and 10 to the financial statements.

Equal Opportunities

Ofgem's Equal Opportunities Policy aims to ensure that no eligible job applicant or employee receives less favourable treatment on grounds of age, disability, sex, race, ethnic or national origin, sexual orientation, religion or religious affiliation or because the employee works part-time.

At the end of the financial year:

- 0.3 per cent of all staff were known to be disabled,
- 45 per cent of all staff were women,
- 40 per cent of staff in managerial grades were women,
- 26 per cent of senior civil service members in Ofgem were women,
- 16 per cent of staff were known to be of ethnic minority origin, and
- staff known to be of ethnic minority origin in the managerial grades was 14 per cent.

The policy statement describing Ofgem's equal opportunity framework is available to provide guidance for all employees.

Communities

Ofgem seeks to support its employees who commit personal time or funds to help charities, community activities or voluntary public activities. For example, special leave may be requested for acting as a school governor, a magistrate or an employment tribunal panel member.

A number of events, organised by charities, have also taken place at Ofgem.

Management Commentary

Income Generation

In 2006-07 cash of £48.2m was received in respect of licence fees and other income mainly from property rental income. Of this, £12.2m was transferred to DTI in respect of the costs of energywatch. Ofgem had an operating income of £38.9m as follows:

Cash receipts:

licence fees	£44.7m
additional deferred licence fees in year	£0.6m
property and other receipts	£2.9m
	£48.2m

Less:

cash transferred to DTI for energywatch	£12.2m
opening debtors	£1.0m
closing deferred licence fees	£3.6m

Add:

closing debtors	£1.6m
opening deferred licence fees	£5.9m
Operating Income	£38.9m

In addition to operating income of £38.9 million, public funds were provided to meet the cost of work undertaken in respect of the Climate Change Levy (£0.6 million).

A saving of £557k from licence fees has been made during 2006-07. This will be offset against future licence fee charges as determined under Ofgem's RPI-X cost regime.

Spending

Total operating costs amounted to £39.5 million. Three areas of expenditure absorbed 83 per cent of the total, staff costs (47 per cent), contractors (15 per cent) and accommodation (21 per cent). Capital expenditure in the year totalled £0.8 million in respect of furniture, office and computer equipment.

Output

Ofgem's financial performance in pursuit of its objectives is detailed in the Statement of Operating Costs by Departmental Aim and Objectives on page 27.

During 2006-07, additional expenditure, as compared to Ofgem's Corporate Plan budgets, was incurred for the objectives of regulating networks effectively, helping protect the security of Britain's energy supplies, and helping to tackle fuel poverty. The expenditure related to additional work on the Distribution Price Control Review, Offshore Wind and the Consumer First project. Expenditure on each of the remaining four objectives was below the Corporate Plan budget and this related to reduced staff levels and lower consultancy costs. Reviews of these and other projects can be found in the Ofgem Annual Report, which is published separately and available from Ofgem's website (www.ofgem.gov.uk).

Budgets and Liquidity

Ofgem's budget is approved by Parliament following a consultation process with industry and other interested parties. For 2006-07, Parliament approved a resource budget of £39.830 million, a capital budget of £1.0 million and a net cash requirement of £7.617 million. In addition, DTI directed that a sum of £12.246 million should be collected on behalf of energywatch; this amount was transferred to DTI, in full.

Reconciliation between resource outturn to the resource budget outturn

	2006-07 £000s	2005-06 £000s
Net Resource Outturn (Estimates)	646	594
Net Operating Costs (Accounts)	646	594
Resource Budget Outturn (Budget)	646	594
Of which:		
Departmental Expenditure Limits (DEL)	646	594
Annually Managed Expenditure (AME)	–	–

A Contingency Fund advance of £10.0 million was drawn down to provide short term liquidity until the first receipt of licence fees. This was fully repaid in September 2006.

The net cash requirement outturn of £4.921 million is lower than the Estimate net cash requirement of £7.617 million due to an increased focus on working capital management during the year, and lower deferred licence fees.

An amount of £2.7 million due to be surrendered to the Exchequer will be retained to fund operations in 2007-08 until adequate licence fee income is received.

Finance and Provisions

Statutory examining and testing services provided by Ofgem laboratories at Leicester were outsourced to SGS UK Ltd. in January 2003. Some costs of this change, particularly redundancy and continuing pension liabilities, have fallen to Ofgem and these have required provisions to be made which now total £0.348 million. From 1 April 2006 Ofgem transferred its metrology activities to the National Weights and Measures Laboratory (NWML) under an administrative arrangement. Responsibility for the metrology duties and existing liabilities remain with Ofgem. A full transfer of responsibility to NWML is planned under future legislative change.

Other early retirement provision totalling £1.205 million relates to the costs of pensions for individuals who have retired early from Ofgem.

A provision of £0.474 million is included within the accounts in respect of the unfunded pension liabilities which fall to Ofgem for a previous Chief Executive, and a Director General.

The balance sheet at 31 March 2007 shows negative Taxpayer's Equity of £3.831 million. This reflects the inclusion of liabilities falling due in future years which are to be financed mainly by drawings from the UK Consolidated Fund. Such drawings will be from grants of Supply approved annually by Parliament to meet Ofgem's Net Cash Requirement. Further detail is provided in Note 1.14 to the financial statements.

Business Focus for the Future

There is currently a significant review of energy policy in Britain and across Europe. Whilst Ofgem has retained the seven core themes described earlier, they will be reviewed later in the year to take account of any relevant developments.

The European Commission's Strategic Energy Review and planned legislative package set an important new course for delivering truly competitive energy markets across Europe. The new European Union renewables target and the Government's Energy White Paper and draft Climate Change Bill will ensure that environmental considerations remain at the heart of future energy policy.

There will also be major changes to the way in which consumer interests are represented in the energy sector as well as new opportunities for consumers to engage more actively with the climate change agenda. It is in this area that Ofgem will examine how households that generate clean energy can benefit from exporting electricity back into the grid.

The Department of Trade and Industry has been consulting on an Energy Review. The review addresses how the UK will take action to achieve real progress in emissions reductions by 2020 and the goal of cutting carbon emissions by 60 per cent by 2050. Ofgem is committed to using its powers and influence to help meet this challenge.

Ofgem has been subject to a sustainable development review performed by the Sustainable Development Commission. The wide ranging review covered both our duties as a regulator and our internal office progress towards sustainability targets. The outcome will be published in a series of publications during May and June 2007.

Ofgem has a long standing commitment to better regulation in all our activities. Better regulation principles are not only applied to policies but also to the way in which we develop them. The supply licence review, for example, proposes substantial benefits to suppliers in terms of reduced administrative burdens and lower costs. Also, the 'Consumer First' project addresses domestic consumers and ensures that their priorities are reflected in Ofgem's future approach, especially in relation to sustainability considerations. Better regulation is not only about policy development. It is also about running Ofgem's operations as efficiently and effectively as possible. The RPI-3 cost control is giving an ongoing incentive to reduce costs in real terms. Further details are shown below.

In February 2004 it was announced that Ofgem would impose a cost control regime (RPI-X) on itself for a period of five years commencing from April 2005. The process is independently overseen by the Audit Committee chaired by Jayne Scott, supported by Chiene and Tait, providers of Ofgem's internal audit service. The Audit Committee concluded that the cost control regime should be set at RPI-3 per cent and this was agreed by the Authority. In April 2007, the Audit Committee reviewed the regime operation and concluded that it was working efficiently and to the benefit of licence payers. It was also recommended that the 2006-07 saving, which at year-end was £0.6 million, should be used to reduce licence fees in 2007-08. The corresponding saving in 2005-06, and licence fee reduction in 2006-07, was £2.9 million. An amount of £3.0 million continues to be retained under RPI-X year-end flexibility.

Remuneration report

Remuneration Committee

The Remuneration Committee consists of non-executive members of the Authority who are appointed by ordinary resolution of the Authority for a term of not more than one year. Members may be reappointed. The Remuneration Committee is chaired by Sir John Mogg, Chairman of the Authority. Other members are Jayne Scott, Chairman of the Audit Committee and Sir Keith Stuart until December 2006. John Wybrew, a non-executive member of the Authority, was appointed to the Remuneration Committee and attended his first meeting in April 2007. The Chief Executive attends as an observer and the Chief Operating Officer provides a secretariat function.

The Committee's role is to review and approve the pay award and the level of any bonus for Senior Management Team members and consider other matters relating to the pay and performance of senior Ofgem staff. Performance pay and bonus awards are made within the parameters set by the Cabinet Office for the Senior Civil Service following recommendations by the Senior Salaries Review Body. The committee also reviews succession planning.

Service contracts

Remuneration of senior members is set out in their contracts and subject to annual review in line with awards recommended by the Senior Salaries Review Body. Senior members of Ofgem, apart from Sir John Mogg, are all permanent members of staff. The notice period for all senior members of Ofgem does not exceed six months.

The arrangements for early termination of senior members are made in accordance with the service contract of the relevant individual. Each contract provides for a payment in lieu of notice on early termination based on the provisions of the Civil Service Compensation Scheme.

Each executive member participates in a bonus scheme which is in line with Senior Salaries Review Body recommendations. The bonus is based on the individual's performance. Bonus payments are non-consolidated and non-pensionable.

Non-executive members, apart from the Chairman of the Authority, have fixed-term appointments not exceeding three years. These appointments are renewable. Remuneration and appointments are set by the Secretary of State for Trade and Industry after consulting the Chairman. Their remuneration is by payment of an honorarium of £20,000 per annum. They have no entitlement to performance related pay or pension entitlements. Compensation in the event of early termination is at the discretion of the Secretary of State. The non-executive Chairman of the Authority, Sir John Mogg, has a five year appointment which commenced on 1 October 2003. His remuneration details are set out below.

Salary and pension entitlements

The salary, pension entitlements and the value of any taxable benefits in kind of the most senior members of Ofgem during 2006-07 were as follows:

Remuneration	2006-07			2005-06		
	Salary, including performance pay	Pension entitlement/ allowances	Benefits in kind	Salary, including performance pay	Pension entitlement/ allowances	Benefits in kind
	£000	£000	Nearest £100	£000	£000	Nearest £100
Alistair Buchanan <i>Chief Executive</i>	215 – 220	N/A	N/A	190 – 195	N/A	N/A
Roy Field <i>Chief Operating Officer</i>	125 – 130	N/A	N/A	120 – 125	N/A	N/A
David Gray <i>Managing Director</i>	160 – 165	35	N/A	150 – 155	26	N/A
Sarah Harrison <i>Managing Director</i>	115 – 120	N/A	N/A	110 – 115	N/A	N/A
Steve Smith <i>Managing Director</i>	155 – 160	N/A	N/A	135 – 140	N/A	N/A
Non-executive members of the Authority						
Sir John Mogg	95 – 100	30	8,900	95 – 100	30	5,600

'Salary' includes gross salary; performance pay or bonuses; overtime; reserved rights to London weighting or London allowances; recruitment and retention allowances; private office allowances and any other allowance to the extent that it is subject to UK taxation.

In addition to the honoraria paid to the non-executive directors, which are included in salaries, they are also entitled to receive expenses.

'Pension entitlement/allowances' relates to an allowance paid to senior staff who have chosen to take extra salary to invest in a pension scheme of their choice rather than participate in a Civil Service pension. Sir John Mogg and David Gray have opted out of the PCSPS and Ofgem make no pension contributions on their behalf but their salary reflects contributions that would otherwise have been made.

'Benefits in kind' covers any monetary benefits provided by the employer and treated by the Inland Revenue as a taxable emolument. Payments outlined above were net of tax and the tax amounts were paid over to HM Revenue and Customs. Travel arrangements for Sir John Mogg fell into this category.

Other non-executive members of the Authority who were remunerated by payment of an honorarium

	Honorarium 2006-07	Honorarium 2005-06
Robin Bidwell	£20,000	£20,000
Miriam Greenwood	£20,000	£20,000
Judith Hanratty	£20,000	£20,000
Jayne Scott	£20,000	£20,000
Sir Keith Stuart	£14,139*	£20,000
Leonard Waverman	£20,000	£20,000
John Wybrew	£20,000	£20,000
George Yarrow	£6,667*	–

* part-year pro-rata

Pension Benefits	Real increase in pension and related lump sum at age 60	Accrued Pension at age 60 at 31 March 2007 and related lump sum	CETV at 31 March 2007	CETV at 31 March 2006	Real increase in CETV	Employer's contribution to partnership pension account
	£000	£000	£000	£000	£000	Nearest £100
Alistair Buchanan <i>Chief Executive</i>	0 – 2.5	5 – 10	81	58	19	N/A
Roy Field <i>Chief Operating Officer</i>	2.5 – 5.0 plus 10 – 12.5 lump sum	55 – 60 plus 170 – 175 lump sum	1,206	1,085	79	N/A
David Gray <i>Managing Director</i>	N/A	N/A	N/A	N/A	N/A	N/A
Sarah Harrison <i>Managing Director</i>	0 – 2.5	10 – 15	141	126	10	N/A
Steve Smith <i>Managing Director</i>	0 – 2.5	10 – 15	105	90	12	N/A
Non-executive member of the Authority						
Sir John Mogg	N/A	N/A	N/A	N/A	N/A	N/A

The following salary and pension details are provided in accordance with the 2006-07 Government Financial Reporting Manual issued by HM Treasury and EPN notice 156 issued by Cabinet Office.

Civil Service Pensions

Pension benefits are provided through the CSP arrangements. From 1 October 2002, civil servants may be in one of three statutory based 'final salary' defined benefit schemes (classic, premium, and classic plus). The schemes are unfunded with the cost of benefits met by monies voted by Parliament each year. Pensions payable under classic, premium, and classic plus are increased annually in line with changes in the Retail Prices Index. New entrants after 1 October 2002 may choose between membership of premium or joining a good quality 'money purchase' stakeholder arrangement with a significant employer contribution (partnership pension account).

Employee contributions are set at the rate of 1.5 per cent of pensionable earnings for classic and 3.5 per cent for premium and classic plus. Benefits in classic accrue at the rate of 1/80th of pensionable salary for each year of service. In addition, a lump sum equivalent to three years' pension is payable on retirement. For premium, benefits accrue at the rate of 1/60th of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum (but members may give up (commute) some of their pension to provide a lump sum). Classic plus is essentially a variation of premium, but with benefits in respect of service before 1 October 2002 calculated broadly in the same way as in the classic.

The partnership pension account is a stakeholder pension arrangement. The employer makes a basic contribution of between 3 per cent and 12.5 per cent (depending on the age of the member) into a stakeholder pension product chosen by the employee from a selection of approved products. The employee does not have to contribute but where they do make contributions, the employer will match these up to a limit of 3 per cent of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8 per cent of pensionable salary to cover the cost of centrally-provided risk benefit cover (death in service and ill health retirement).

Further details about the CSP arrangements can be found at the website www.civilservice-pensions.gov.uk

Cash Equivalent Transfer Values

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures, and from 2003-04 the other pension details, include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the CSP arrangements and for which the CS Vote has received a transfer payment commensurate to the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost.

CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries. Prior to 2006-07, CETVs were calculated using club terms. From 2006-07, CETVs are calculated using non-club terms. 2005-06 CETVs have been restated accordingly.

Real increase in CETV

This reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Alistair Buchanan
Accounting Officer
4 May 2007

Statement of Accounting Officer's Responsibilities

Under the Government Resources and Accounts Act 2000, Ofgem is required to prepare resource accounts for each financial year, in conformity with a Treasury direction, detailing the resources acquired, held, or disposed of during the year and the use of resources by Ofgem during the year.

The resource accounts are prepared on an accruals basis and must give a true and fair view of the state of affairs of Ofgem at the year-end and of the net resource outturn, resources applied to objectives, recognised gains and losses and cash flows for the financial year.

The Treasury has appointed the Chief Executive as Ofgem's Accounting Officer with responsibility for preparing Ofgem's accounts and for transmitting them to the Comptroller and Auditor General.

In preparing the resource accounts, the Accounting Officer is required to comply with the Government Financial Reporting Manual prepared by the Treasury and, in particular, to:

- observe all relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis
- make judgements and estimates on a reasonable basis
- state whether applicable accounting standards, as set out in the Government Financial Reporting Manual, have been followed, and disclose and explain any material departures in the accounts, and
- prepare the financial statements on a going concern basis.

The relevant responsibilities of the Accounting Officer (including his responsibility for the propriety and regularity of public finances for which an Accounting Officer is answerable, for the keeping of proper records and for safeguarding Ofgem's assets) are set out in the Accounting Officers' Memorandum, issued by the Treasury and published in Government Accounting.

Statement on Internal Control

1. Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control that supports the achievement of Ofgem's policies, aims and objectives, whilst safeguarding the public funds and departmental assets for which I am personally responsible, in accordance with the responsibilities assigned to me in Government Accounting.

Ofgem is a non-ministerial government department governed by the Gas and Electricity Markets Authority. In fulfilling its obligations Ofgem works closely with the Department of Trade and Industry (DTI), Department for Environment, Food and Rural Affairs (DEFRA) and energywatch.

2. The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level, rather than to eliminate all risk of failure to achieve policies, aims and objectives. It can therefore only provide reasonable, and not absolute, assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of departmental policies, aims and objectives; to evaluate the likelihood of those risks being realised and the impact should they be realised; and to manage them efficiently, effectively and economically. The system of internal control has been in place in Ofgem for the year ended 31 March 2007 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

3. Capacity to handle risk

Ofgem's risk management strategy sets out why risk management is important; the mechanisms in place to enable Ofgem to manage risk; information on how to identify, assess and manage risks; and details of the roles and responsibilities individuals have to ensure risks are managed effectively. In April 2006 the risk management strategy was updated and approved by the Audit Committee.

Under the strategy, risk is embedded in policymaking, planning and delivery. Directors are responsible for ensuring the proper management of risks within their own directorates and cascading implementation of the risk management strategy within their directorates. The strategy is available to all staff via the intranet.

4. The risk and control framework

Ofgem's current work is being undertaken at a time of profound review of energy policy in Britain and across Europe. This includes:

1. The European Commission's Strategic Energy Review and planned legislative package
2. The new European Union renewables target
3. The Government's Energy White Paper and draft Climate Change Bill
4. Major changes to the way in which consumer interests are represented in the energy sector
5. New opportunities for consumers to engage more actively with the climate change agenda.

In order to respond effectively to these challenges Ofgem recognises and embraces the key role risk management can play in assisting the organisation in delivery of complex objectives, all of which are subject to risk.

Ofgem's stated aim is to implement best practice risk management procedures in all areas of our work to ensure that our strategy is kept up-to-date with current good practice. Ofgem is seeking to embed risk management into the culture of the organisation by embracing best practice in the way we work. Managers view risk management as an integral part of their job and the Senior Management Team keep the top risks faced by the organisation under regular strategic review. Our basic principles can be summarised as follows:

1. A proactive stance to risk management,
2. Consistency in how we assess and manage risks,
3. Cross-cutting risks will be identified, with risk owners empowered to manage risks across internal boundaries,
4. Proportionate actions will be taken when managing risks,
5. A robust approach to risk management will be taken, and
6. Appropriate risk-taking will be encouraged with an innovative approach to policy making and service delivery.

The key elements of Ofgem's risk management strategy for identifying, evaluating and controlling risk are as follows:

1. Project, policy and programme managers create and maintain a risk register (a bottom-up approach),
2. Risks are assessed and given a risk rating using a combination of their likelihood and impact,
3. All risks identified in quarterly reports are reviewed by senior managers during the quarterly review process,
4. Early warning indicators are in place for the most important risks - damage to Ofgem's reputation, policy errors and legal,
5. Audit Committee considers risk on a regular basis,
6. Senior Management Team and Directors review strategic risks and update, where necessary, Ofgem's risk framework (a top-down approach),
7. Annually, the Authority identify top risks based on the risk framework, and
8. In all cases, all risks, once identified, are managed by a risk manager who will be responsible for applying practical and proportionate countermeasures.

5. Review of effectiveness

As Accounting Officer, I also have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within Ofgem who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Authority, the Audit Committee and a plan to address weaknesses identified through internal or external audit, and ensure continuous improvement of the system is in place. Of the thirteen recommendations made by internal audit and due for implementation by 31 January 2007, nine have been fully implemented by year-end, two have been partially implemented and two have been superseded.

During the year, a number of key activities have been undertaken to monitor and enhance Ofgem's internal control environment:

- Ofgem's risk strategy was updated and approved by the Audit Committee in April 2006;
- The highest rated risks were reviewed by Senior Management Team and the Authority;
- An Audit Committee workshop was undertaken in March 2007. The workshop facilitated discussion and review of a number of topics including HM Treasury's new Audit Committee Handbook and risk management;
- Regular one to one meetings were held between the Accounting Officer and Managing Directors to review resources, progress towards set objectives and to identify and evaluate associated risks;
- Updated internal control statements require all Directors to consider and report on all aspects of financial and risk management, and other governance control issues in their own area;
- Business continuity plans have been updated, ensuring that key activities can continue effectively following a disruption; and
- Internal auditors have reviewed Ofgem's risk management processes and procedures, assessing Ofgem's rating as 'Substantial Assurance'.

In maintaining and reviewing the effectiveness of the system of internal control the role of Ofgem's bodies which inform my review are detailed below:

The **Authority**, which meets at least ten times a year to consider the plans and overall strategic direction of Ofgem. The top risks to Ofgem are reviewed, based on the risk framework, on an annual basis;

The **Senior Management Team** which meets on a weekly basis to manage all resource and operational issues. SMT is corporately responsible for owning Ofgem's risk management strategy. The top risks are agreed, owned and addressed by SMT members;

An **Audit Committee** comprising non-executive members of the Authority which reports directly to the Authority is responsible for advising the Authority as to the adequacy of risk management procedures and processes in Ofgem;

Internal Audit (provided under contract) offers an independent assurance on the managerial, financial and operational controls. They are independent of management and work to standards defined in the Government Internal Audit Standard. Internal audit reports are a key element of the Accounting Officer's review of the effectiveness of the system of internal control. The Audit Committee agrees a rolling programme of audit for each forthcoming year according to the Committee's priorities;

The **Head of Internal Audit** presents a yearly review of the audit programme, including an assessment of general risk, and an opinion on the adequacy and effectiveness of Ofgem's system of internal control together with recommendations for improvement. Overall assurance levels available are Full, Substantial, Limited and Nil. The report for the year ended 31 March 2007 has an overall opinion of 'Substantial Assurance'; and

Directors are responsible for ensuring that risks have been properly identified and assessed across all their work areas, paying particular attention to cross-cutting risks. They are responsible for agreeing their key risk return for their work areas and for ensuring that each policy/project/programme manager is actively addressing the risks in their command and escalating risks up to Director-level as appropriate.

No significant internal control problems have arisen during the financial year.

The format of this statement complies with HM Treasury guidance as set out in Government Accounting Chapter 21.3.

Alistair Buchanan
Accounting Officer
4 May 2007

The Certificate and Report of the Comptroller and Auditor General to the House of Commons

I certify that I have audited the financial statements of the Office of Gas and Electricity Markets for the year ended 31 March 2007 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, the Operating Cost Statement and Statement of Total Recognised Gains and Losses, the Balance Sheet, the Cashflow Statement and the Statement of Operating Costs by Departmental Aim and Objectives and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Accounting Officer and auditor

The Accounting Officer is responsible for preparing the Annual Report, which includes the Remuneration Report, and the financial statements in accordance with the Government Resources and Accounts Act 2000 and HM Treasury directions made thereunder and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer's Responsibilities.

My responsibility is to audit the financial statements and the part of the Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000. I report to you whether, in my opinion, certain information given in the Annual Report, which comprises the introduction, the sustainability report, the management commentary and the Remuneration Report is consistent with the financial statements. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

In addition, I report to you if the Department has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by HM Treasury regarding remuneration and other transactions is not disclosed.

I review whether the Statement on Internal Control reflects the Department's compliance with HM Treasury's guidance, and I report if it does not. I am not required to consider whether this statement covers all risks and controls, or to form an opinion on the effectiveness of the Department's corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. I consider the implications for my certificate if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinions

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the Accounting Officer in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Department's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinions

Audit Opinion

In my opinion:

- the financial statements give a true and fair view, in accordance with the Government Resources and Accounts Act 2000 and directions made thereunder by HM Treasury, of the state of the Department's affairs as at 31 March 2007, and the net cash requirement, net resource outturn, net operating cost, operating costs applied to objectives, recognised gains and losses and cashflows for the year then ended;
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government Resources and Accounts Act 2000; and
- information given within the Annual Report, which comprises the introduction, the sustainability report, the management commentary and the Remuneration Report is consistent with the financial statements.

Audit Opinion on Regularity

In my opinion, in all material respects, the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Report

I have no observations to make on these financial statements.

John Bourn

Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria
London SW1W 9SP

9 May 2007

Statement of Parliamentary Supply

Summary of Resource Outturn 2006-07 (£000s)

	2006-07			2006-07			Net total outturn compared with estimate: saving/(excess)	2005-06
	Estimate			Outturn				Net total
	Gross expenditure	A in A	NET TOTAL	Gross expenditure	A in A	NET TOTAL		
Request for Resources 1 Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry (Note 2)	39,130	(39,127)	3	38,863	(38,862)	1	2	1
Request for Resources 2 Expenditure in connection with the Climate Change Levy (Note 2)	700	–	700	645	–	645	55	593
Total resources	39,830	(39,127)	703	39,508	(38,862)	646	57	594
Non-operating cost A in A (Note 7)	–	(50)	(50)	–	–	–	50	(16)

Net cash requirement 2006-07

	Note	Estimate	Outturn	Net total outturn compared with estimate: saving/(excess)	Prior year outturn
Net cash requirement	4	7,617	4,921	2,696	–

Summary of income payable to the Consolidated Fund

(In addition to appropriations in aid, the following income relates to Ofgem and is payable to the Consolidated Fund (cash receipts being shown in italics and figures in £000s))

	Note	Forecast 2006-07		Outturn 2006-07	
		Income	<i>Receipts</i>	Income	<i>Receipts</i>
Cash surrenderable to the Consolidated Fund	5	–	–	257,695	257,695

Explanations of variances between Estimate and Outturn are given in the Management Commentary.

The notes on pages 28 to 46 form part of these accounts

Operating Cost Statement*for the year ended 31 March 2007 (£000s)*

		2006-07		2005-06	
	Note	Staff costs	Other Costs	Income	
Administration costs:					
Requests for Resources 1:					
Staff costs	10	18,610			16,511
Non-Staff administration costs	11		20,198		19,424
Operating Income	9			(38,807)	(35,934)
Request for Resources 2:					
Non-Staff administration costs	11		645		593
Programme costs					
Request for Resources 1:					
Expenditure	12		55		117
Income	12			(55)	(117)
Totals		<u>18,610</u>	<u>20,898</u>	<u>(38,862)</u>	<u>594</u>
Net operating costs	3			<u>646</u>	<u>594</u>

All income and expenditure are derived from continuing operations

Statement of Total Recognised Gains and Losses*for the year ended 31 March 2007 (£000s)*

	2006-07	2005-06
Net operating cost	(646)	(594)
Net (loss)/gain on revaluation of tangible fixed assets	(19)	4
Overnight change in pension liability	–	(29)
Actuarial loss on revaluation of pension liabilities	(59)	(31)
Total recognised losses for the financial year	<u>(724)</u>	<u>(650)</u>

The notes on pages 28 to 46 form part of these accounts.

Balance Sheet*as at 31 March 2007 (£000s)*

	Note	31 March 2007	31 March 2006
Fixed assets:			
Tangible assets	13	<u>3,996</u>	<u>4,113</u>
		3,996	4,113
Current assets:			
Debtors	14a	3,838	2,592
Cash at bank and in hand	15	<u>2,695</u>	<u>3,244</u>
		6,533	5,836
Creditors (amounts falling due within one year)	16a	<u>(9,411)</u>	<u>(12,812)</u>
Net current liabilities		(2,878)	(6,976)
Total assets less current liabilities		(1,118)	(2,863)
Creditors (amounts falling due after more than one year)	16a	(2,922)	(3,239)
Provisions for liabilities and charges	17	<u>(1,553)</u>	<u>(1,359)</u>
Total net liabilities before pension liability		(3,357)	(7,461)
Pension liabilities	17	<u>(474)</u>	<u>(407)</u>
Total net liabilities		(3,831)	(7,868)
Taxpayers' equity:			
General fund	18	(3,835)	(7,899)
Revaluation reserve	19	<u>4</u>	<u>31</u>
		(3,831)	(7,868)

Alistair Buchanan
Accounting Officer
4 May 2007

The notes on pages 28 to 46 form part of these accounts.

Cash Flow Statement*for year ended 31 March 2007 (£000s)*

	Note	2006-07	2005-06
Net cash (outflow)/inflow from operating activities	20a	(4,167)	2,373
Capital expenditure and financial investment	20b, 20c	(754)	(726)
Receipts due to the Consolidated Fund which are outside the scope of the Department's activities	8, 29	255,000	–
Payments of amounts due to the Consolidated Fund		(256,647)	(2,632)
Financing	20d	6,019	1,597
(Decrease)/Increase in cash in the period	20e	(549)	612

The notes on pages 28 to 46 form part of these accounts.

Statement of Operating Costs by Departmental Aim and Objectives*for the year ended 31 March 2007 (£000s)***AIM: To protect consumers' interests, wherever possible by promoting effective competition and only where necessary through regulation.**

Objective	2006-07			2005-06		
	Gross	Income	Net total	Gross	Income	Net total
1. Creating and sustaining competition	10,940	(10,940)	–	11,748	(11,748)	–
2. Regulating networks effectively	17,976	(17,976)	–	14,791	(14,791)	–
3. Helping to protect the security of Britain's energy supplies	2,446	(2,446)	–	2,450	(2,450)	–
4. Providing a leading voice in Europe	2,015	(2,015)	–	2,273	(2,273)	–
5. Helping to protect the environment	4,512	(3,866)	646	4,249	(3,655)	594
6. Helping tackle fuel poverty	1,288	(1,288)	–	1,134	(1,134)	–
7. Better Regulation	331	(331)	–	–	–	–
Net operating cost	39,508	(38,862)	646	36,645	(36,051)	594

An explanation of the methodology for allocating costs to objectives is given in Note 1.11 and Note 21.

The notes on pages 28 to 46 form part of these accounts.

Notes to the departmental resource accounts

1. Statement of accounting policies

These financial statements have been prepared in accordance with the 2006-07 Government Financial Reporting Manual (FReM) issued by HM Treasury. The accounting policies contained in the FReM follow UK generally accepted accounting practice for companies (UK GAAP) to the extent that it is meaningful and appropriate to the public sector.

In addition to the primary statements prepared under UK GAAP, the FReM also requires Ofgem to prepare two additional primary statements. The Statement of Parliamentary Supply and supporting notes show outturn against Estimate in terms of the net resource requirement and the net cash requirement. The Statement of Operating Cost by Departmental Aim and Objectives and supporting notes analyse the Department's income and expenditure by the objectives agreed with Ministers.

Where the FReM permits a choice of accounting policy, the accounting policy which has been judged to be most appropriate to Ofgem's particular circumstances for the purpose of giving a true and fair view has been selected. The Department's accounting policies have been applied consistently in dealing with items considered material in relation to the accounts.

1.1 Accounting convention

These accounts have been prepared under the historical cost convention, modified to include the revaluation of fixed assets at their value to the business by reference to their current costs.

1.2 Tangible fixed assets and depreciation

Tangible assets have been stated at current cost using indices provided by the Office of National Statistics. Leasehold improvements are not revalued.

Depreciation is provided at rates calculated to write off tangible fixed assets by equal instalments over their estimated useful lives, after allowance for residual value. Asset lives are within the following ranges:

Leasehold improvements	Life of the lease
Office equipment, furniture and fittings	5 years
Computers and IT equipment	3 years

The minimum level for the capitalisation of tangible fixed assets is £2,000. The grouping of assets below the threshold has been restricted to IT items only.

1.3 Provisions

Ofgem makes provision for liabilities and charges where, at the balance sheet date, a legal or constructive liability exists (i.e. a present obligation from past events exists), where the transfer of economic benefits is probable and a reasonable estimate can be made.

Where the time value of money is material, Ofgem discounts the provision to its present value using a discount rate of 2.2 per cent, the Government's standard rate. Each year the financing charges in the Operating Cost Statement include the adjustments to amortise one year's discount and restate liabilities to current price levels.

1.4 Operating income

Operating income is income that relates directly to the operating activities of Ofgem. It comprises principally licence fees and fees and charges for services provided on a full cost basis.

Notes to the departmental resource accounts *(continued)*

Since all licence costs are recovered via the licence fees, and these are invoiced in two tranches during the year based on estimated costs, any over recovery is treated as deferred income within Creditors and any under recovery as accrued income within Debtors.

1.5 Administration and programme expenditure

The Operating Cost Statement is analysed between administration and programme costs. Administration costs reflect the costs of running Ofgem. These include both administration costs and associated operating income. Income is analysed in the notes between that which, under the administrative cost-control regime, is allowed to be offset against gross administration costs in determining the outturn against the administration cost limit, and that operating income which is not. Programme costs reflect Ofgem's costs in respect of the Fossil Fuel Levy. The classification of expenditure and income as administration or as programme follows the definition of administration costs set by HM Treasury.

1.6 Capital charge

A charge, reflecting the cost of capital utilised by Ofgem, is included in the operating costs. The charge is calculated at the real rate set by HM Treasury, 3.5 per cent for 2006-07, on the average carrying amount of all assets less liabilities, except for:

- cash balances with the Office of the Paymaster General (OPG) where the charge is nil, and
- liabilities for amounts to be surrendered to the Consolidated Fund, where the credit is nil.

1.7 Foreign exchange

Transactions which are denominated in a foreign currency are translated into sterling at the rate of exchange ruling on the date of each transaction, except where rates do not fluctuate significantly, in which case an average rate for the period is used.

1.8 Pensions

Past and present employees are covered by the provisions of the Principal Civil Service Pension Scheme (PCSPS), which is non-contributory and unfunded. Liability for payment of future benefits is a charge to the PCSPS. Departments, agencies and other bodies covered by the PCSPS meet the cost of pension cover provided for the staff they employ by payment of charges calculated on an accruing basis. Liability for payment of future benefits is a charge on the PCSPS. There is a separate scheme statement for the PCSPS as a whole.

Ofgem's former Chief Executive and Director General have separate pension arrangements that are broadly analogous with the PCSPS. The arrangements provide for a defined benefit, unfunded scheme. However, unlike the PCSPS, a pension liability is included in the accounts as required under FRS17.

1.9 Early departure costs

Ofgem is required to meet the additional cost of benefits beyond the normal PCSPS benefits in respect of employees who retire early. Ofgem provides in full for this cost when the early retirement programme has been announced and is binding on Ofgem.

Notes to the departmental resource accounts *(continued)*

1.10 Value Added Taxation

Value Added Tax (VAT) is accounted for in the accounts, in that amounts are shown net of VAT except:

- irrecoverable VAT is charged to the Operating Cost Statement and included under the heading relevant to the type of expenditure, and
- irrecoverable VAT on the purchase of an asset is included in the capitalised purchase cost of the asset.

The amount due to, or from, HM Revenue and Customs in respect of VAT is included within Debtors and Creditors within the Balance Sheet.

1.11 The Statement of Parliamentary Supply and the Statement of Operating Costs by Departmental Aim and Objectives

The information contained in the Statement of Parliamentary Supply and associated notes is based on the Request for Resources information that will form part of parliamentary approval processes.

The Statement of Operating Costs by Departmental Aim and Objectives has been prepared from the underlying books and records. Where possible costs have been directly attributed to each objective. Overhead costs have been attributed based on the appropriate cost driver.

1.12 Operating leases

Rentals due under operating leases are charged to the Operating Cost Statement over the lease term on a straight-line basis, or on the basis of actual rentals payable which fairly reflects the usage. Future payments, disclosed at Note 23, "Commitments under leases", are not discounted.

1.13 Comparative amounts

Comparative amounts are restated where necessary to conform to current presentation.

1.14 Going concern

The balance sheet at 31 March 2007 shows a negative taxpayers equity of £3.831m. This reflects the inclusion of liabilities falling due in future years, which are to be financed mainly by drawings from the UK Consolidated Fund. Such drawings will be from grants of supply approved annually by Parliament, to meet Ofgem's Net Cash Requirement. Under the Government Resources and Accounts Act 2000, no money may be drawn from the Fund other than required for the service of the specified year or retained in excess of that need. All unspent monies, including those derived from Ofgem's income, are surrenderable to the Fund.

In common with other government departments, the future financing of Ofgem's liabilities is accordingly to be met by future grants of Supply and the application of future income, both to be approved annually by Parliament. Such approval for amounts required for 2007-08 has already been given and there is no reason to believe that future approvals will not be forthcoming. It has accordingly been considered appropriate to adopt a going concern basis for the preparation of these financial statements.

1.15 Contingent liabilities

In addition to contingent liabilities disclosed in accordance with FRS 12, Ofgem discloses for parliamentary reporting and accountability purposes certain contingent liabilities where the likelihood of a transfer of economic benefit is remote. These comprise all items (whether or not they arise in the normal course of business) over £250,000 (or lower, where required by specific statute or where material in the context of resource accounts) which are required by the FReM to be noted in the resource accounts.

Notes to the departmental resource accounts *(continued)*

Where the time value of money is material, contingent liabilities which are required to be disclosed under FRS 12 are stated at discounted amounts and the amount reported to Parliament separately noted. Contingent liabilities that are not required to be disclosed by FRS 12 are stated at the amounts reported to Parliament.

2. Analysis of net resource outturn by function

	2006-07					Estimate	Net total outturn compared with Estimate	2005-06
	Outturn							
	Admin	Other current	Gross resource expenditure	A in A	Net total			
£000	£000	£000	£000	£000	£000	£000		
Request for Resources 1								
Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry	38,808	55	38,863	(38,862)	1	3	2	1
Request for Resources 2								
Expenditure in connection with the Climate Change Levy	645	–	645	–	645	700	55	593
Resource outturn	39,453	55	39,508	(38,862)	646	703	57	594

3. Reconciliation of Outturn to net operating cost and against Administration Budget**3(a) Reconciliation of net resource outturn to net operating cost**

	Note	2006-07	2005-06
		£000	£000
Net Resource Outturn	2	646	594
Prior period adjustments		–	–
Non supply income (CFERs)	5	–	–
Non supply expenditure		–	–
Net operating cost		646	594

Notes to the departmental resource accounts *(continued)*

3(b) Outturn against final Administration Budget

	Note	2006-07		2005-06	
		Budget	Outturn	Budget	Outturn
		£000	£000	£000	£000
Gross Administration Budget	2	39,620	39,453	38,942	36,528
Income allowable against the Administration Budget	2	(38,917)	(38,807)	(38,241)	(35,934)
Net outturn against the Administration Budget		703	646	701	594

4. Reconciliation of resources to cash requirement

	Note	Estimate	Outturn	Net total outturn compared with estimate: saving/ (excess)
		£000	£000	£000
Resource Outturn	2	703	646	57
Capital:				
• Acquisition of fixed assets	13	1,000	759	241
• Investments		-	-	-
Non-operating A-in-A:				
• Proceeds of fixed asset disposals	20b	(50)	-	(50)
Accruals adjustments:				
• Non-cash items	11	255	67	188
• Depreciation		(1,000)	(764)	(236)
• Other non-cash items		(45)	-	(45)
• New provisions and adjustments to provisions		(5)	(697)	692
• Movement in working capital		5,768	4,415	1,353
• Use of provision	17	991	495	496
Excess cash receipts surrenderable to the Consolidated Fund	5	-	-	-
Net cash requirement		7,617	4,921	2,696

The explanation for the variance between the outturn net cash requirement and the Estimate can be found in the Management Commentary.

Notes to the departmental resource accounts *(continued)***5. Analysis of income payable to the Consolidated Fund**

In addition to appropriations in aid, the following income relates to Ofgem and is payable to the Consolidated Fund (cash receipts being shown in italics)

	Note	Forecast 2006-07		Outturn 2006-07	
		Income	Receipts	Income	Receipts
		£000	£000	£000	£000
Operating income and receipts – excess A in A		-	-	-	-
Other operating income and receipts not classified as A in A	6	-	-	-	-
		-	-	-	-
Non operating income and receipts not classified as A in A	7	-	-	-	-
Surplus supply surrenderable to the Consolidated Fund	16	-	-	2,695	2,695
Other amounts collectable on behalf of the Consolidated Fund	8	-	-	255,000	255,000
Excess cash surrenderable to the Consolidated Fund	4	-	-	-	-
Total income payable to the Consolidated Fund		-	-	257,695	257,695

6. Reconciliation of income recorded within the Operating Cost Statement to operating income payable to the Consolidated Fund

	Note	2006-07	2005-06
		£000	£000
Operating Income	9	38,862	36,051
Income authorised to be appropriated in aid		(38,862)	(36,051)
Operating Income payable to the Consolidated Fund	5	-	-

7. Non-operating income – Excess A in A

	Note	2006-07	2005-06
		£000	£000
Proceeds on disposal of fixed assets	20b	-	16
Allowable A in A		(50)	(50)
Excess A in A		-	-

8. Other amounts collectable on behalf of the Consolidated Fund

	Note	Income	Receipts
		£000	£000
Fossil Fuel Levy	29	255,000	255,000

Notes to the departmental resource accounts *(continued)*

9. Income and appropriations in aid

9.1 Operating income

Operating income not appropriated in aid (i.e. surrenderable to the Consolidated Fund) is analysed for resource budget purposes between that which is included in public expenditure and that which is not (see note 6). In 2006-07, there was no operating income not classified as A in A.

	2006-07		2005-06	
	A in A	Income	A in A	Income
	£000	£000	£000	£000
Administrative income:				
Fees and charges to external customers	34,783	34,783	31,938	31,938
Fees and charges to other departments	4,024	4,024	3,996	3,996
	38,807	38,807	35,934	35,934
Programme income:				
Fossil Fuel Levy	55	55	117	117
Total	38,862	38,862	36,051	36,051

9.2 Operating income analysis

An analysis of income from services provided to external and public sector customers is as follows:

	2006-07			2005-06		
	Income	Full costs	(Deficit)	Income	Full costs	(Deficit)
	£000	£000	£000	£000	£000	£000
Administration income						
Gas and Electricity:						
Licence fees (external)	34,783	35,429	(646)	31,911	32,505	(594)
Other	4,024	4,024	-	4,023	4,023	-
Subtotal	38,807	39,453	(646)	35,934	36,528	(594)
Programme income:						
Fossil Fuel Levy	55	55	-	117	117	-
	38,862	39,508	(646)	36,051	36,645	(594)

All of the above operating income was appropriated in aid. Appropriations in Aid represent income due to Ofgem that can be retained for offset against other public expenditure. This contrasts with CFERs, which are remitted by Ofgem to the Consolidated Fund.

Other income includes:	2006-07	2005-06
	£000	£000
Rent received:		
Department for Environment, Food and Rural Affairs (DEFRA)	3,659	3,923
Other departments	332	73
Miscellaneous	33	27
	4,024	4,023

Miscellaneous income includes licence application fees, and other minor items.

Notes to the departmental resource accounts *(continued)*

10. Staff numbers and related costs

Staff costs comprise

	2006-07			2005-06
	Permanently employed staff	Others	Total	Total
	£000	£000	£000	£000
Wages and salaries	13,045	716	13,761	12,731
Social security costs	1,267	–	1,267	1,184
Other pension costs	2,580	–	2,580	2,329
Other staff costs	1,002	–	1,002	312
Total	17,894	716	18,610	16,556
Less recoveries in respect of outward secondments	–	–	–	(45)
Total net costs*	17,894	716	18,610	16,511

* Of the total, no charge has been made to capital

The Principal Civil Service Pension Scheme (**PCSPS**) is an unfunded multi-employer defined benefit scheme but Ofgem is unable to identify its share of the underlying assets and liabilities. A full actuarial valuation was carried out as at 31 March 2003. Details can be found in the resource accounts of the **Cabinet Office: Civil Superannuation** (www.civilservice-pensions.gov.uk).

For 2006-07, employers' contributions of £2,551,000 were payable to the PCSPS (2005-06 £2,305,000) at one of four rates in the range 17.1 per cent to 25.5 per cent (2005-06 16.2 to 24.6 per cent) of pensionable pay, based on salary bands. The contribution rates reflect benefits accruing during 2006-07 to be paid when the member retires, and not the benefits paid during this period to existing pensioners.

Employees can opt to open a partnership pension account, a stakeholder pension with an employer contribution. Employers' contributions of £26,965 (2005-06 £21,361) were paid to one or more of a panel of four appointed stakeholder pension providers. Employer contributions are age-related and range from 3 to 12.5 per cent of pensionable pay. Employers also match employee contributions up to 3 per cent of pensionable pay. In addition, employer contributions of £2,138 (2005-06 £2,276), 0.8 per cent of pensionable pay, were payable to the **PCSPS** to cover the cost of the future provision of lump sum benefits on death in service and ill health retirement of these employees. Contributions due to the **partnership** pension providers at the balance sheet date amounted to zero (2005-06 £2,415).

Average number of persons employed

The average number of whole-time equivalent persons employed during the year is shown in the table below.

Objective	2006-07			2005-06
	Permanently employed staff	Others	Total	Total
Creating and Sustaining competition	93	2	95	104
Regulating networks effectively	117	6	123	103
Helping to protect the security of Britain's energy supplies	17	1	18	16
Providing a leading voice in Europe	14	–	14	17
Helping to protect the environment	39	1	40	37
Helping tackle fuel poverty	13	–	13	8
Better regulation	3	–	3	–
Total	296	10	306	285

Notes to the departmental resource accounts *(continued)***11. Other administration costs**

	Note	<u>2006-07</u>	<u>2005-06</u>
		£000	£000
Rental under operating leases:			
Hire of office equipment		82	107
Other operating leases		5,547	5,510
		<u>5,629</u>	<u>5,617</u>
Non-cash items (see below):			
Auditors' remuneration and expenses*		44	46
Depreciation	13	764	742
Loss on disposal of fixed assets		4	113
Cost of capital charge		(204)	(229)
Diminution in value of fixed assets		89	138
		<u>697</u>	<u>810</u>
Other expenditure:			
Contractors		6,020	5,927
Other accommodation costs		2,885	2,929
Office supplies and services		982	1,040
Travel and subsistence		771	689
Contracted laboratory costs		737	595
Training		501	619
Recruitment		402	657
Telecoms		238	287
Media and Communications		222	218
Library Services		178	194
Hospitality		96	109
Other expenditure		788	357
		<u>13,820</u>	<u>13,621</u>
Provisions (non-cash):			
Provided in year	17	625	398
Provision not required written back	17	(1)	(461)
Unwinding of the discount	17	73	32
Movement in provision		<u>697</u>	<u>(31)</u>
		20,843	20,017
Administration costs			
Request for Resources 1		20,198	19,424
Request for Resources 2		645	593
		<u>20,843</u>	<u>20,017</u>

* There was no auditor remuneration for non-audit work.

Reconciliation of Operating costs to Operating cashflows in the Cashflow Statement and the Statement of Parliamentary Supply

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Non-cash costs (admin)	1,394	779
Less non-cash income	-	-
Total non-cash transactions	<u>1,394</u>	<u>779</u>

Notes to the departmental resource accounts *(continued)*

12. Net programme costs

	2006-07	2005-06
	£000	£000
Fossil Fuel Levy costs	55	117
Programme costs	55	117
Programme income	(55)	(117)
Net programme costs	–	–

Total programme income and expenditure for 2006-07 is reflected in the Operating Cost Statement at £55,000.

13. Tangible fixed assets

	Furniture	Office equipment	Computer equipment	Leasehold works	Total
	£000	£000	£000	£000	£000
Cost or valuation					
At 1 April 2006	380	1,126	1,322	4,295	7,123
Additions	3	483	273	–	759
Disposals	–	(25)	(226)	–	(251)
Revaluations	–	(61)	(32)	2	(91)
At 31 March 2007	383	1,523	1,337	4,297	7,540
Depreciation					
At 1 April 2006	314	456	912	1,328	3,010
Charged in year	20	204	280	260	764
Disposals	–	(21)	(226)	–	(247)
Revaluations	2	6	7	2	17
At 31 March 2007	336	645	973	1,590	3,544
Net book value					
At 31 March 2007	47	878	364	2,707	3,996
Net book value					
At 31 March 2006	66	670	410	2,967	4,113
Asset financing:					
Owned	47	878	364	2,707	3,996
Net book value					
At 31 March 2007	47	878	364	2,707	3,996

Tangible assets have been revalued using appropriate indices.

Ofgem depreciates capitalised leasehold improvement costs over the life of the lease.

Reconciliation of cash flows to tangible fixed asset additions

(Cash flow Statement)

	2006-07	2005-06
	£000	£000
Tangible fixed asset additions	759	656
Creditor for fixed asset additions	(9)	(4)
Creditor reversals	4	90
Cash flows for tangible fixed assets	754	742

Notes to the departmental resource accounts *(continued)***14. Debtors****14(a) Analysis by type**

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Amounts falling due within one year:		
Trade debtors	1,048	475
Accrued income	79	73
Prepayments	2,266	1,597
HM Revenue and Customs (VAT)	273	244
Staff debtors	172	203
At 31 March	<u>3,838</u>	<u>2,592</u>

Staff debtors represent loans outstanding, of which £94,000 relates to season ticket loans for 89 employees; and £78,000 relates to housing advances in respect of 4 employees.

Staff debtors due after more than one year: The balance of £78,000 (2005-06: £105,000) relating to housing advances comprises £66,000 (2005-06: £89,000) which is repayable in instalments after one year.

14(b) Intra-government balances

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Balances with other central government bodies	1,361	403
Balances with local authorities	–	–
Balances with public corporations and trading funds	–	–
Balances with bodies external to government	2,477	2,189
At 31 March	<u>3,838</u>	<u>2,592</u>

15. Cash at bank and in hand

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Balance at 1 April	3,244	2,632
Net change in cash balances	(549)	612
Balance at 31 March	<u>2,695</u>	<u>3,244</u>
The following balances at 31 March are held at:		
Office of HM Paymaster General	2,643	3,225
Commercial banks and cash in hand	52	19
Balance at 31 March	<u>2,695</u>	<u>3,244</u>

Notes to the departmental resource accounts *(continued)*

16. Creditors

16(a) Analysis by type

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Amounts falling due within one year:		
Trade creditors	364	430
Staff creditors	5	76
Deferred licence fees	3,557	5,924
Other Taxation and Social Security	434	379
Leasehold reverse premium	316	316
Accruals and other deferred income	2,040	2,443
Amounts issued from the Consolidated Fund for supply but not spent at year end	2,695	1,597
Excess cash receipts	-	1,647
Consolidated Fund Extra Receipts due to be paid to the Consolidated Fund:		
	received	-
	receivable	-
Balance at 31 March	<u>9,411</u>	<u>12,812</u>
	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Amounts falling due after more than one year:		
Leasehold reverse premium	2,922	3,239
Balance at 31 March	<u>2,922</u>	<u>3,239</u>

When Ofgem entered into a lease on its Millbank headquarters in 2000, it received a leasehold reverse premium from the landlord. The remainder of the reverse premium is £3.238m and will be utilised on a straight-line basis over the lease term up to the first break in the lease, being 23 June 2017.

16(b) Intra-government balances

	Creditors: amounts falling due within one year	Creditors: amounts falling due after more than one year
	£000	£000
Balances with other central government bodies	4,327	-
Balances with local authorities	-	-
Balances with public corporations and trading funds	-	-
Balances with bodies external to government	5,084	2,922
At 31 March 2007	<u>9,411</u>	<u>2,922</u>
Balances with other central government bodies	4,232	-
Balances with local authorities	-	-
Balances with public corporations and trading funds	-	-
Balances with bodies external to government	8,580	3,239
At 31 March 2006	<u>12,812</u>	<u>3,239</u>

Notes to the departmental resource accounts *(continued)***17. Provisions for liabilities and charges**

	Early Retirement	Severance	Total
	£000	£000	£000
Balance at 1 April 2006	1,205	154	1,359
Provided in the year	603	–	603
Unwinding of the discount	73	–	73
Provisions not required written back	–	(1)	(1)
Provisions utilised in the year	(328)	(153)	(481)
Net movement in year	348	(154)	194
Balance at 31 March 2007	1,553	–	1,553
Of which:			
Payable within one year	401	–	401

The total movement in provision in 2006-07 was an increase of £194,000.

The Early Retirement provision relates to the costs of pensions for individuals who have retired early. Ofgem meets the cost of pension payments from its resources until the individual reaches normal retirement age. The provision has been discounted, with the undiscounted amount being £1,749,831.

The Severance cost provision related to a resource review in 2005-06. The provision was fully utilised as at 31 March 2007.

Pension liabilities

	2006-07	2005-06
	£000	£000
Provision at 1 April 2006	407	340
Overnight charge to provision	–	29
Interest cost	22	21
Actual benefit payments	(14)	(14)
Actuarial loss	59	31
Provision at 31 March 2007	474	407
Net movement in year (excluding actuarial loss)	8	36

History of experience losses

	2006-07	2005-06
	£000	£000
Experience (gains)/losses arising on the scheme liabilities	(6)	31
Amount recognised as a percentage of present value of scheme liabilities	(1.2%)	7.6%
Total amount recognised in statement of total recognised gains and losses	59	60
Percentage of present value of the scheme liabilities	12.5%	15%

The pensions provision is in respect of the unfunded pension liabilities which fall to Ofgem for the previous Chief Executive and a Director General. The pension provision is unfunded, with the benefits being paid as they fall due and guaranteed by Ofgem. There is no fund, and therefore no surplus or deficit. Actuarial advice has been sought to ensure that the provision is set at a realistic level.

Notes to the departmental resource accounts *(continued)*

An actuarial valuation was carried out by the Government Actuary's Department (GAD) at 31 March 2007. The major assumptions used by the actuary were:

	At 31 March 2007 % (per annum)	At 31 March 2006 % (per annum)
Inflation assumption	2.75	2.5
Rate of increase in salaries	4.3	4.0
Investment return in excess of price increases	1.8	2.8
Rate of increase for pensions in payment and deferred pensions	2.75	2.5

Analysis of Actuarial Loss	2006-07	2005-06
	<u>£000</u>	<u>£000</u>
Changes in assumptions underlying the present value of scheme liabilities	65	–
Experience (gains)/losses arising on the scheme liabilities	(6)	31
Per statement of total recognised gains and losses	59	31

On 1 April 2005 the discount rate for pension scheme liabilities changed from 3.5% to 2.8% per annum. The impact of this change was an overnight increase in the pension liability of £29,000 as at 1 April 2005. From 31 March 2007, the discount rate for pension scheme liabilities changed to 1.8%. This rate is reflected in the valuation of the pension scheme liability as at 31 March 2007.

18. General Fund

	2006-07		2005-06	
	<u>£000</u>	<u>£000</u>	<u>£000</u>	<u>£000</u>
Balance at 1 April		(7,899)		(5,422)
Net Parliamentary Funding:				
Draw Down	6,019		1,597	
Deemed Supply	1,597		–	
		7,616		1,597
Net transfer from operating activities:				
Net operating cost		(646)		(594)
Excess cash repayable to Consolidated Fund		(2,695)		(3,244)
Non-cash charges:				
Cost of capital	(204)		(229)	
Auditor's remuneration	44		46	
		(160)		(183)
Realised on revaluations and disposals of assets		8		7
Losses relating to pension liabilities		(59)		(60)
Balance at 31 March		(3,835)		(7,899)

19. Revaluation Reserve

	2006-07	2005-06
	<u>£000</u>	<u>£000</u>
Balance at 1 April	31	35
Arising on revaluation during the year (net)	(19)	4
Transferred to General Fund in respect of realised element of the Revaluation Reserve	(8)	(8)
Balance at 31 March	4	31

The Revaluation Reserve reflects the unrealised element of the cumulative balance of indexation and the revaluation adjustments of tangible fixed assets.

Notes to the departmental resource accounts *(continued)*

20. Notes to the Cash Flow Statement

20(a) Reconciliation of operating cost to operating cash flows

		<u>2006-07</u>	<u>2005-06</u>
	Note	£000	£000
Net operating cost	3a	646	594
Adjustments for non-cash transactions	11	(1,394)	(779)
Increase/(decrease) in Debtors	14a	1,246	(1,386)
<i>Less movements in debtors relating to items not passing through the OCS</i>	14a	–	–
Decrease/(increase) in Creditors	16a	3,401	(2,322)
<i>Less movements in creditors relating to items not passing through the OCS</i>	16a	(544)	526
Decrease in long term creditors	16a	317	316
Use of provisions	17	495	678
Net cash outflow/(inflow) from operating activities		<u>4,167</u>	<u>(2,373)</u>

20(b) Analysis of capital expenditure and financial investment

		<u>2006-07</u>	<u>2005-06</u>
	Note	£000	£000
Tangible fixed asset additions	13	754	742
Proceeds on disposal of fixed assets	20c	–	(16)
Net cash outflow from investing activities		<u>754</u>	<u>726</u>

20(c) Analysis of capital expenditure and financial investment by Request for Resources

	Capital expenditure	Loans, etc.	A in A	Net total
	£000	£000	£000	£000
Request for Resources 1				
Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry	754	–	–	754
Request for Resources 2				
Expenditure in connection with the Climate Change Levy	–	–	–	–
Total 2006-07	<u>754</u>	<u>–</u>	<u>–</u>	<u>754</u>
Total 2005-06	<u>656</u>	<u>–</u>	<u>(16)</u>	<u>640</u>

20(d) Analysis of financing

		<u>2006-07</u>	<u>2005-06</u>
	Note	£000	£000
From the Consolidated Fund (Supply) – current year	18	6,019	1,597
Advances from the Contingency Fund		10,000	10,000
Repayments to the Contingency Fund		(10,000)	(10,000)
Net financing		<u>6,019</u>	<u>1,597</u>

Notes to the departmental resource accounts *(continued)***20(e) Reconciliation of Net Cash Requirement to change in cash**

		<u>2006-07</u>	<u>2005-06</u>
	Note	£000	£000
Net cash requirement		(4,921)	–
From the Consolidated Fund (Supply) – current year	20d	6,019	1,597
From the Consolidated Fund (Supply) – prior year	20d	–	–
Amounts paid over to the Consolidated Fund – received in prior year		(1,647)	(2,632)
Excess cash surrenderable to the Consolidated Fund		–	1,647
Amounts due to the Consolidated Fund received and not paid over		–	–
(Decrease)/Increase in cash		<u>(549)</u>	<u>612</u>

21. Notes to the Statement of Resources by Departmental Aim and Objectives

Ofgem's capital is employed exclusively for administrative purposes and its attribution to objectives is in the same proportion as the related gross administrative cost. Where costs cannot be directly attributed to each objective, they have been classed as overhead and attributed based on the underlying cost driver, in accordance with the Department's normal management accounting practices. Overhead costs were apportioned according to the direct headcount for each objective.

22. Capital commitments

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Contracted capital commitments at 31 March for which no provision has been made	–	–

23. Commitments under leases**Operating leases**

Commitments under operating leases to pay rentals during the year following the year of these accounts are given in the table below, analysed according to the period in which the lease expires.

	<u>2006-07</u>	<u>2005-06</u>
	£000	£000
Obligation under operating leases comprise:		
Land and buildings:		
Expiry within 1 year	–	–
Expiry after 1 year but not more than 5 years	99	99
Expiry thereafter	5,704	5,704
	<u>5,803</u>	<u>5,803</u>
Other:		
Expiry within 1 year	11	8
Expiry after 1 year but not more than 5 years	7	111
Expiry thereafter	–	–
	<u>18</u>	<u>119</u>

Notes to the departmental resource accounts *(continued)*

24. Other financial commitments

Ofgem had not entered into any non-cancellable contracts (which are not operating leases) as at 31 March 2007.

25. Contingent liabilities disclosed under FRS 12

From time to time Ofgem will be subject to legal challenge and judicial review of decisions made in the normal course of its business as regulator of the gas and electricity markets. Legal judgements could give rise to liabilities for legal costs but these cannot be quantified as the outcome of proceedings would be unknown and there is therefore considerable uncertainty as to the nature and extent of any subsequent liability.

As at 31 March 2007 there were no contingent liabilities requiring disclosure.

26. Financial instruments

FRS 13, *Derivatives and Other Financial Instruments*, requires disclosure of the role which financial instruments have had during the period in creating or changing the risks an entity faces in undertaking its activities. Because of the largely non-trading nature of its activities and the way in which government departments are financed, Ofgem is not exposed to the degree of financial risk faced by business entities. Moreover, financial instruments play a much more limited role in creating or changing risk than would be typical of the listed companies to which FRS 13 mainly applies. Ofgem has very limited powers to borrow or invest surplus funds and except for relatively insignificant forward purchases of foreign currency, financial assets and liabilities are generated by day-to-day operational activities and are not held to change the risks facing Ofgem in undertaking its activities.

As permitted by FRS 13, debtors and creditors which mature or become payable within 12 months from the balance sheet date have been omitted from the currency profile.

Liquidity risk

Ofgem operates on a full cost recovery basis and is financed primarily by licence fee income and has no borrowings. Specific and limited areas of operation are, for reasons of public policy, directly funded by grants of supply approved annually by Parliament. The extent to which licence fee and other income may be raised and retained for use in operations (Appropriated in Aid) is also approved by annual vote of Parliament, along with further grants of supply needed to meet Ofgem's Net Cash Requirement. Ofgem is not therefore exposed to significant liquidity risks.

Interest rates and foreign currency risks

Ofgem has no material deposits, and all material assets and liabilities are denominated in Sterling, so it is not exposed to any significant interest rate or foreign currency risks.

Fair values

There is no material difference between the book values and fair values of Ofgem's financial assets and liabilities as at 31 March 2007.

Notes to the departmental resource accounts *(continued)*

27. Related Party Transactions

Ofgem transferred £12.246m to DTI in respect of the costs of energywatch.

Ofgem sublets part of its Millbank premises to DEFRA, provides financial and payroll services to Postcomm, and administers the Northern Ireland Renewables Obligation on behalf of the NI Authority for Energy Regulation. Income received in year was £3.7m from DEFRA, £70k from Postcomm and £194k from NI Authority for Energy Regulation.

Ofgem has also had a small number of transactions with other government departments and central government bodies.

None of the Authority members, key managerial staff or other related parties has undertaken any material transactions with Ofgem during the year.

28. Post balance sheet events

There were no reportable post balance sheet events between the balance sheet date, and the 9 May 2007, the date when the Accounting Officer despatched the accounts to HM Treasury. The financial statements do not reflect events after this date.

29. Fossil Fuel Levy

Ofgem is responsible for setting, collecting and administering the Fossil Fuel Levy (FFL) via commercial bank accounts. The Department of Trade and Industry (DTI) has overall responsibility for the making of regulations governing the FFL. Under the Electricity Act 1989, the Secretary of State made five Orders (three now remain) requiring the then Regional Electricity Companies (RECs) in England and Wales to contract for certain amounts of renewable generating capacity. This was known as the Non Fossil Fuel Obligation (NFFO). The FFL was created in 1990 to finance NFFO. Similar Regulations came into force in Scotland in 1996, and are the responsibility of the Scottish Executive.

The Sustainable Energy Act 2003 created a mechanism by which sums of money could be transferred from the England and Wales levy account to the Consolidated Fund. The Secretary of State for Trade and Industry is under a duty to spend the amount for the purpose of promoting the use of energy from renewable sources. A parallel provision has been included in the Energy Bill for the Scottish Executive relating to the Scotland levy account.

Cash receipts can also be treated as hereditary revenue when they are received by virtue of statutory authority. Section 1 of the Civil List Act 1952 requires hereditary revenues to be paid into the Consolidated Fund. On 22 September 2006 and 20 March 2007, £160m and £95m respectively, were transferred to the Consolidated Fund from the England and Wales account on this basis.

The balance held at 31 March 2007 in the England and Wales account was £30 million and the Scotland account held £59 million.

In accordance with the FReM issued by HM Treasury, Ofgem is required to disclose any monies held on behalf of third-parties. All monies collected through the FFL have in the past fallen into this category. Prior to 2006-07 under Government Accounting rules, the account balances were defined as third-party assets where Ofgem nor the Government more generally had any direct beneficial interest. They were therefore not included in our Resource Account.

From 2006-07, the surplus over and above the core third-party balance of £30 million in the England and Wales account is now treated as CFER income in our Resource Account and reflected in the Statement of Parliamentary Supply. The change in treatment arises due to an increased certainty that the surplus will go to the consolidated fund. This does not score against resource expenditure. The total balance held in the Scotland levy account continues to be treated as monies held on behalf of third-parties.

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