

# **Office of Gas and Electricity Markets**

## **Resource Accounts 2007-08**

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**Office of Gas and Electricity  
Markets  
Resource Accounts  
2007-08**

**(For the year ended 31 March 2008)**

*Ordered by the House of Commons to be printed  
30 April 2008*

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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 2007 to 31 March 2008. It should be read in conjunction with the Ofgem Annual Report for 2007-08, which is published separately and available from Ofgem's website ([www.ofgem.gov.uk](http://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.

A new Energy Bill will implement the legislative aspects of the Energy White Paper: meeting the energy challenge. The Bill was announced in the Queen's Speech on 6 November 2007 and was introduced in the House of Commons on 10 January 2008. The Bill is currently proceeding through Parliament.

In fulfilling its obligations Ofgem works closely with the Department for Business, Enterprise and Regulatory Reform (BERR), 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. The Consumers, Estate Agents and Redress Act 2007 made provision for the establishment of the National Consumer Council and the abolition of energywatch and a number of other consumer bodies. Upon commencement, Ofgem will work closely with the new body.

### 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 2007-2012 identified seven themes:

1. Creating and sustaining competition,
2. Regulating networks effectively,
3. Helping to protect the security of Britain's energy supplies,

4. A leading voice in Europe,
5. Helping to achieve sustainable development,
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. In February 2008 he was reappointed for a further five years until September 2013. 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. He left the Authority in December 2007, although he remains a member of staff for a set period of time under normal business appointment rules.

Dr Andrew Wright, Managing Director, Markets, appointed in January 2008.

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

Steve Smith, Managing Director, Networks, appointed in January 2008. He was previously 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. In February 2008 he was reappointed. His current appointment ends in September 2013.

Dr Robin Bidwell joined the Authority as a non-executive member in February 2003. In February 2008 he was reappointed. His current appointment ends in February 2010.

Miriam Greenwood joined the Authority as a non-executive member in May 2004. In May 2007 she was reappointed. Her current appointment ends in May 2010.

Judith Hanratty joined the Authority as a non-executive member in January 2005. In December 2007 she was reappointed. Her current appointment ends in December 2009.

Jayne Scott joined the Authority as a non-executive member in May 2004. In May 2007 she was reappointed. Her current appointment ends in May 2010.

Professor Leonard Waverman joined the Authority as a non-executive member in May 2002. He left the Authority in May 2007.

John Wybrew joined the Authority as a non-executive member in May 2004. In May 2007 he was reappointed. His current appointment ends in May 2009.

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	13/13	–	2/2	–
Dr Robin Bidwell	12/13	–	–	6/6
Miriam Greenwood	13/13	–	–	–
Judith Hanratty	12/13	4/4	–	5/6
Jayne Scott	10/13	4/4	2/2	–
Professor Leonard Waverman *	1/1	–	–	–
John Wybrew	13/13	4/4	2/2	5/6
Professor George Yarrow	13/13	–	–	5/6

(\*) term of appointment ended May 2007

Professor Nigel Brandon was offered a Non-Executive appointment to the Authority by the Secretary of State. He attended the January 2008 meeting, but decided not to proceed given the possibility of a conflict of interest.

On governance issues, the Authority has introduced a corporate structure with committees having clear terms of reference. They provide the necessary structure to ensure that there is a strong framework of internal control throughout the organisation.

Working closely with the European Commission and others, the Chairman, Sir John Mogg, has continued to contribute fully 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 Regulators (ERGEG).

The Chairman and Non-Executives have played a full part in Authority business through their attendance and contributions at Authority meetings and meetings of committees of the Authority as indicated. They have attended Ofgem seminars, briefing sessions and an open session of the Authority to which the public were

invited. Non-executives have had regular contacts with Ofgem teams dealing with those areas of special responsibility assigned to each of them by the Chairman. In addition to the work of the Audit and Remuneration Committees, and the Sustainable Development Committee, some non-executives have also taken part in assessing and formulating price control proposals during the course of the year involving meetings with the gas distribution industry.

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 Authority governance and procedures. These were designed to improve its efficiency and effectiveness. The Authority has taken several opportunities to meet with interested parties, and held its September meeting in Glasgow, using the occasion to host a meeting with senior energy interests from the private and public sectors in Scotland.

During the year, the Authority reviewed its rules and procedures in respect of delegated powers with minor amendments and updating. It agreed a resolution to delegate to Managing Directors certain levels of decision-making on more minor infringements of licence conditions or procedures. The Authority also reviewed its policies and procedures in respect of requests for information under the Freedom of Information Act 2000.

### **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 following paragraphs set out Ofgem's response to HM Treasury's Corporate Governance Code for Central Government Departments.

### **Audit Committee**

The Audit Committee is chaired by Jayne Scott. The Committee comprises the Chairman and Non-Executive directors Judith Hanratty and John Wybrew. 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 2007-08, including a workshop which facilitated discussion and review of a number of topics including risk management and Ofgem's environmental programmes.

### **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. A detailed report was first prepared in 2006 on Ofgem's sustainable development policies, priorities and activities. The 2007 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 supply; and in supporting improvement in all aspects of the environment.

### **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 16 to 19.

**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 £42,000. There was no auditor remuneration (actual or notional) for non-audit work.

During the year, the House of Lords Select Committee on Regulators took evidence from Ofgem and other regulators on economic regulatory work. The National Audit Office (NAO) were invited by the Select Committee to conduct a review of the way in which Impact Assessments are used by regulators. The NAO report was included in full as an Appendix to the Select Committees report which was published in November 2007.

In March 2008, the National Audit Office published a report 'Protecting consumers? Removing retail price controls.' The report evaluates the regulators that removed price controls and how effectively they are monitoring the market. In the press statement accompanying his report Tim Burr stated that "The removal of price controls is an important step in the development of competition in these markets, but it is not the end of the story. The regulators need to be vigilant, and be prepared to use their other powers when necessary, to ensure genuine competition is present and that it is working to serve consumers."

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.

The Energy Bill, currently proceeding through Parliament, will ensure the long term delivery of our energy and climate change strategy. The Bill provides for the implementation of an offshore electricity transmission licensing and regulatory regime based on competitive tendering to award offshore electricity transmission licences.

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 BERR and the Devolved Administrations on the long-term reforms of the RO which are due to be implemented in April 2009. Ofgem will also continue to work with Government on the development of its energy efficiency programmes.

In 2008, Ofgem will implement the next phase of the EEC – the Carbon Emissions Reduction Target (CERT). Ofgem will also implement new IT systems to administer the environmental programmes.

On 1 November 2007 Ofgem published its second Sustainable Development Report. The report sets out the progress Ofgem has made in encouraging the development of a more sustainable energy industry and the actions to be taken during 2007-08.

### Sustainable development action plan (Internal Ofgem Operations)

In September 2007 Ofgem introduced an internal sustainability development action plan. The sustainability work focuses on five key areas:

- *Climate change and energy efficiency.* To minimise our consumption of natural resources, including water, as far as reasonably and economically practicable, and to incorporate long term strategies for energy efficiency into planning and capital purchases,
- *Waste management and recycling.* To reduce waste, increase the proportion of waste that is recycled and eliminate our use of landfill sites for general office waste,
- *Procurement.* To promote a purchasing policy which will give preference, as far as practical, to those products and services which cause the least harm to the environment by incorporating specific environmental requirements into contracts with principal suppliers,
- *Travel.* To encourage travel options that minimise the environmental impact, and to promote the use of technology, such as videoconferencing, as alternatives to travel where practical,
- *People.* To seek to embed the principle of sustainable development through increasing awareness of sustainability responsibilities among staff and for all who work with us.

Targets will be set annually in order to achieve continuous improvement and our environmental performance will be reported on annually.

In setting this new sustainability challenge, Ofgem is building on what has already been achieved over the past few years. Ofgem gained ISO14001 certification for environmental management in 2002 and have retained this each year since.

In September 2007 Ofgem also gained Energy Efficiency Accreditation Status from the National Energy Foundation. Part of the requirements of this award were to demonstrate that energy initiatives have been implemented, senior management were involved and staff were energy efficient aware.

We have also implemented many energy saving initiatives including a combined heat and power unit, which significantly reduces our carbon emissions. 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' has also been introduced which has led to an increase in the amount of recycling and reduced waste collection.

## **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 2007-08 Ofgem paid 98 per cent of undisputed bills within these deadlines.

## **Employees**

### ***Training and Development***

Ofgem's most important investment is in its people. There is an active policy of recruiting and retaining high calibre staff.

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 new management development programme, known as Generating Excellence in Management (GEM). This is a skills development programme for leaders and managers, including all members of the SMT and Directors, and will be a key enabler in building a high level of people management competence.

This commitment is reflected in expenditure: £0.542 million was spent on training during 2007-08.

### ***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:

- 1 per cent of all staff were known to be disabled,
- 45 per cent of all staff were women,
- 42 per cent of staff in managerial grades were women,
- 30 per cent of senior civil service members in Ofgem were women,
- 18 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 15 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 2007-08 income of £39.2 million was received in respect of licence fees and other income mainly from property rental income. In addition, £10.783 million was received from licence fee payers and transferred to BERR in respect of the costs of energywatch.

In addition to operating income of £39.2 million, public funds were provided to meet the cost of work undertaken in respect of the Climate Change Levy (£0.7 million).

A saving of £924k from licence fees has been made during 2007-08. This will be offset against future licence fee charges as determined under Ofgem's RPI-X cost regime.

### Spending

Total operating costs amounted to £39.907 million. Three areas of expenditure absorbed 84 per cent of the total, staff costs (48 per cent), contractors (13 per cent) and accommodation (23 per cent). Capital expenditure in the year totalled £0.8 million in respect of office equipment and information technology.

### Output

Ofgem's financial performance in pursuit of its objectives is detailed in the Statement of Net Operating Costs by Departmental Aim and Objectives on page 30. 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](http://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 2007-08, Parliament approved a resource budget of £40.186 million, a capital budget of £1.0 million and a net cash requirement of £1.849 million. A Spring Supplementary Estimate allowed Ofgem to reclassify expenditure in connection with environmental programmes from Request for Resources RfR2 to RfR1. This change better reflects Ofgem's responsibilities for the administration of environmental programmes.

In addition, BERR directed that a sum of £10.783 million should be collected on behalf of energywatch; this amount was transferred to BERR, in full.

### Reconciliation between resource outturn and the resource budget outturn

	2007-08 £000s	2006-07 £000s
<b>Net Resource Outturn (Estimates)</b>	695	646
Net Operating Costs (Accounts)	695	646
<b>Resource Budget Outturn (Budget)</b>	695	646
<b>Of which:</b>		
Departmental Expenditure Limits (DEL)	695	646
Annually Managed Expenditure (AME)	–	–

A financial penalty of £41.6 million was imposed on National Grid plc in February 2008. The penalty was in respect of National Grid plc abusing its dominant position in the market in Great Britain for the provision of domestic-sized gas meters. This was an infringement of Section 18 of the Competition Act 1998 and Article 82 of the EC Treaty. National Grid plc must either settle the penalty or initiate appeal proceedings by

21 May 2008.

A financial penalty of £25,000 was imposed on Northern Gas Networks Limited in February 2008. The penalty was in respect of a breach of performance standards relating to connections. This was in contravention of its obligations in special licence condition D10 (2) (b) (c) and (e) of its gas transporters licence. The penalty was received in February 2008 and paid over to the Exchequer.

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 August 2007.

The net cash requirement outturn of £0.376 million is lower than the Estimate net cash requirement of £1.849 million, due to higher than budgeted provisions being raised and capital creditors exceeding planned levels.

An amount of £1.5 million due to be surrendered to the Exchequer will be retained to fund operations in 2008-09 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 £0.295 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 the Energy Bill which is currently proceeding through Parliament.

Other early retirement provision totalling £1.362 million relates to the costs of pensions for individuals who have retired early from Ofgem.

A provision of £0.578 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 2008 shows negative Taxpayer's Equity of £4.345 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.

An announcement by the Chancellor in the 2008 Budget Report confirmed that International Financial Reporting Standards (IFRS) will be adopted by Ofgem and other departments from 2009-10. Shadow IFRS accounts will be produced for 2008-09. A project team has been set up to ensure that next year's shadow resource accounts are IFRS compliant.

### **Business Focus for the Future**

There is currently significant new energy legislation being developed at both EU and UK level. The EU's 2020 targets on reducing greenhouse gas emissions and increasing renewables, and new liberalising legislative measures, open up the possibility for significant strides to be made in Europe's energy policy. UK legislation on energy, climate change and planning will also be vitally important in setting the course for domestic energy policy.

Whilst Ofgem has retained the seven core themes described earlier, they take into account Ofgem's developing work on making the gas and electricity sectors more sustainable.

In July 2007, the Competition Commission allowed in part an appeal against a decision by the Authority to reform the gas offtake regime for Great Britain's high-pressure National Transmission System. E.ON UK Limited appealed the Authority's decision to direct modifications to the Uniform Network Code. British Gas

Trading Limited intervened in support of E.ON's appeal. The Competition Commission ordered the Authority to pay E.ON 50 per cent of its costs incurred in the appeal, British Gas Trading 25 per cent of its costs, and the Competition Commission 100 per cent of its costs. The total of these costs and Ofgem's own costs amounted to £767,000.

In late 2007 and early 2008 wholesale prices increased due to a range of factors but mainly due to high oil prices. For industrial and commercial customers who had not entered into fixed price contracts their energy costs have increased significantly. The domestic market remains the most competitive in Europe and the scope to make savings by switching to the lowest cost supplier remains significant. Given the price rises, Ofgem will continue to facilitate efforts by the Government and industry to target fuel poverty measures on those most in need. Ofgem will also continue a broader programme of work as part of the Social Action Strategy to protect the interests of vulnerable customers.

In December 2007, Ofgem published final proposals for the gas distribution price control review. These were accepted by the gas distribution networks (GDNs). Work is now planned to implement the final proposals through the modification of GDN licences.

In February 2008, Ofgem launched an investigation into the markets in electricity and gas for households and small businesses. The decision to conduct the probe was in response to growing public concern about whether the market is working effectively and recent movements in energy prices. Initial findings from the probe will be published ahead of winter 2008.

In March 2008, Ofgem announced plans to review the 20-year old RPI-X regime governing the regulation of the gas and electricity networks. The two-year review will examine whether the current approach will continue to deliver customers reliable, well-run networks with good service at reasonable prices amid growing investment challenges faced by the energy networks in the future.

Ofgem will continue to work with the Department of Business, Enterprise and Regulatory Reform (BERR) in developing the regulatory and licensing regime for offshore transmission networks. Offshore networks are important as they will transmit electricity from marine renewable plant to the onshore network. They have the potential both to strengthen security of supply and contribute to a lower carbon energy system.

Major reforms are expected to the onshore transmission network to promote fairer access for new and renewable generators. Ofgem is currently working with BERR to conduct a joint review of the regime. Work will also continue on the new regulatory arrangements that may be necessary to extend the electricity transmission network to the Scottish Islands to enable the development of renewable energy for export to the mainland.

Distributed energy has the potential to make a large contribution towards reducing carbon emissions from the energy sector. Ofgem took forward work with BERR, on addressing the barriers to distributed energy within the current marketing and licensing arrangements. Possible options for reducing barriers will be developed in more detail for consideration.

Ofgem will continue work to establish effective metering competition and to facilitate the introduction of more advanced or smarter forms of metering for domestic and business customers within the framework of a competitive metering market.

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, delivered major benefits to suppliers through reduced administrative burdens and lower costs. The distribution licence review is expected to provide a shorter and easier licence to use and our approach to enforcing sectoral, competition and consumer protection law will be reviewed to assess how it is working in practice. 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 overleaf.

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 2008, 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 2007-08 saving, which at year-end was £0.924 million, should be used to reduce licence fees in 2008-09. The corresponding saving in 2005-06 and 2006-07, was £2.9 million and £0.6 million respectively. All of these savings were achieved at the same time as achieving the objectives and targets set out in the corporate strategy. 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 John Wybrew. 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.

### Salary and pension entitlements

The following information has been subject to external audit.

The salary, pension entitlements and the value of any taxable benefits in kind of the most senior members of Ofgem during 2007-08 were as follows:

Remuneration	2007-08			2006-07		
	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>	245 – 250	N/A	N/A	215 – 220	N/A	N/A
Roy Field <i>Chief Operating Officer</i>	145 – 150	N/A	N/A	125 – 130	N/A	N/A
David Gray (to December 2007*) <i>Managing Director</i>	185 – 190	40	N/A	160 – 165	35	N/A
Dr Andrew Wright (from January 2008**) <i>Managing Director</i>	125 – 130	N/A	N/A	N/A	N/A	N/A
Sarah Harrison <i>Managing Director</i>	145 – 150	N/A	N/A	115 – 120	N/A	N/A
Steve Smith <i>Managing Director</i>	185 – 190	N/A	N/A	155 – 160	N/A	N/A
<b>Non- executive members of the Authority</b>						
Sir John Mogg	100 – 105	30	9,200	95 – 100	30	8,900

\*David Gray ceased to be a senior member of staff in December 2007, although he remains a member of staff for a set period of time under normal business appointment rules. The table above includes his remuneration for the entire financial year.

\*\*Annual equivalent salary: 165-170

'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 2007-08	Honorarium 2006-07
Robin Bidwell	£20,000	£20,000
Miriam Greenwood	£20,000	£20,000
Judith Hanratty	£20,000	£20,000
Jayne Scott	£20,000	£20,000
Leonard Waverman	£5,000*	£20,000
John Wybrew	£20,000	£20,000
George Yarrow	£20,000	£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 2008 and related lump sum	CETV at 31 March 2008	CETV at 31 March 2007	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	122	81	24	N/A
Roy Field <i>Chief Operating Officer</i>	0 – 2.5 plus 5 – 10 lump sum	60 – 65 plus 175 – 180 lump sum	1,411	1,206	48	N/A
David Gray (to December 2007*) <i>Managing Director</i>	N/A	N/A	N/A	N/A	N/A	N/A
Dr Andrew Wright (from January 2008) <i>Managing Director</i>	0 – 2.5	0 – 2.5	10	N/A	9	N/A
Sarah Harrison <i>Managing Director</i>	0 – 2.5	10 – 15	204	141	22	N/A
Steve Smith <i>Managing Director</i>	0 – 2.5	10 – 15	147	105	16	N/A
<b>Non-executive member of the Authority</b>						
Sir John Mogg	N/A	N/A	N/A	N/A	N/A	N/A

\* David Gray ceased to be a senior member of staff in December 2007, although he remains a member of staff for a set period of time under normal business appointment rules.

### 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 Business, Enterprise and Regulatory Reform 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 an appointment which commenced on 1 October 2003 for five years. In February 2008 it was announced that he had been reappointed for a further five years until September 2013. His remuneration details are set out in the above table.

The salary and pension details above are provided in accordance with the 2007-08 Government Financial Reporting Manual issued by HM Treasury and EPN notice 210 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](http://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.

**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  
25 April 2008

## 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 Managing Public Money published by the Treasury.

## 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 Managing Public Money.

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 for Business, Enterprise and Regulatory Reform (BERR), 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 2008 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.

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 change in Britain's energy markets with the shift towards developing more sustainable and low carbon energy solutions. New targets to reduce carbon and increase renewables will be set both by the Climate Change Bill in Parliament and by the European Commission's Renewables Directive. Ofgem's approach to these challenges includes the following work:

- Develop a new regime to connect offshore wind to the transmission system,
- Promote the development of distributed energy and microgeneration,
- Conduct major reforms to the onshore transmission network to promote fairer access for new and renewable generators, and
- Through our Consumer First project, to gain a deeper insight into consumer priorities now and in the future.

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:

- A proactive stance to risk management,
- Consistency in how we assess and manage risks,
- Cross-cutting risks will be identified, with risk owners empowered to manage risks across internal boundaries,
- Proportionate actions will be taken when managing risks,
- A robust approach to risk management will be taken, and
- 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:

- Project, policy and programme managers create and maintain a risk register (a bottom-up approach),
- Risks are assessed and given a risk rating using a combination of their likelihood and impact,
- All risks identified in quarterly reports are reviewed by senior managers during the quarterly review process,
- Audit Committee considers risk on a regular basis, including in 2007, a review of Ofgem's strategic risks,
- Senior Management Team and Directors review strategic risks and update, where necessary, Ofgem's risk framework (a top-down approach),
- Annually, the Authority identify top risks based on the risk framework, and
- 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 23 recommendations made by internal audit and due for implementation by 31 January 2008, 18 have been fully implemented by year-end, 4 have been partially implemented and 1 has been superseded.

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

- Ofgem's strategic risks were reviewed by the Senior Management Team, the Audit Committee and the Authority;
- An Audit Committee workshop was undertaken in September 2007. The workshop facilitated discussion and review of a number of topics including Ofgem's management of the risk of fraud in the environmental programmes we administer, and risk management;

- A new in-house project and risk management training course was developed and run for staff from December 2007;
- Internal procedures were reviewed and, where necessary, strengthened to ensure that personal information is adequately safeguarded;
- 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 mitigation of strategic risks, assessing Ofgem's rating as Substantial.

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 2008 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.

*Alistair Buchanan*  
Accounting Officer  
25 April 2008

## **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 2008 under the Government Resources and Accounts Act 2000. These comprise the Statement of Parliamentary Supply, the Operating Cost Statement and Statement of 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, the information which comprises the introduction, the sustainability report and the management commentary, included in the Annual 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. This other information comprises the unaudited part of the Remuneration Report. 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

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 2008, 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 which comprises the introduction, the sustainability report and the management commentary included within the Annual Report, is consistent with the financial statements.

## 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.

*T J Burr*  
Comptroller and Auditor General  
National Audit Office  
151 Buckingham Palace Road  
Victoria  
London SW1W 9SS

29 April 2008

## Statement of Parliamentary Supply

### Summary of Resource Outturn 2007-08 (£000s)

	2007-08						Restated	
	Estimate			Outturn			2006-07	
	Gross expenditure	A in A	NET TOTAL	Gross expenditure	A in A	NET TOTAL	Net total outturn compared with estimate: saving/(excess)	Net total
Request for resources 1 Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry and expenditure in connection with environmental programmes (Note 2)	40,186	39,483	703	39,907	39,212	695	8	646
Total resources	40,186	39,483	703	39,907	39,212	695	8	646
Non-operating cost A in A (Note 7)	-	(50)	(50)	-	-	-	50	-

### Net cash requirement 2007-08

	Note	Estimate	Outturn	Net total outturn compared with estimate: saving/(excess)	Prior year outturn
Net cash requirement	4	1,849	376	1,473	4,921

### 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 2007-08		Outturn 2007-08	
		Income	<i>Receipts</i>	Income	<i>Receipts</i>
Cash surrenderable to the Consolidated Fund	5	-	-	121,496	121,496

The notes on pages 31 to 49 form part of these accounts.

**Operating Cost Statement***for the year ended 31 March 2008 (£000s)*

		2007-08		Restated 2006-07	
	Note	Staff costs	Other costs	Income	
<b>Administration costs</b>					
<b>Request for Resources 1:</b>					
Staff costs	10	19,198			18,610
Other administration costs	11		20,709		20,843
Operating income	9			(39,212)	(38,807)
<b>Programme costs</b>					
<b>Request for Resources 1:</b>					
Staff costs	12	–			55
Income	12			–	(55)
<b>Totals</b>		<u>19,198</u>	<u>20,709</u>	<u>(39,212)</u>	<u>646</u>
<b>Net operating cost</b>	3			<u>695</u>	<u>646</u>

All income and expenditure are derived from continuing operations.

**Statement of Recognised Gains and Losses***for the year ended 31 March 2008 (£000s)*

	Note	2007-08	2006-07
Net loss on revaluation of tangible fixed assets	13	–	(19)
Actuarial loss on revaluation of pension liabilities	17	(97)	(59)
<b>Recognised losses for the financial year</b>		<u>(97)</u>	<u>(78)</u>

The notes on pages 31 to 49 form part of these accounts.

**Balance Sheet***as at 31 March 2008 (£000s)*

	Note	31 March 2008	31 March 2007
<b>Fixed assets:</b>			
Tangible assets	13	4,012	3,996
		<b>4,012</b>	<b>3,996</b>
<b>Current assets:</b>			
Debtors	14a	4,220	3,838
Cash at bank and in hand	15	1,471	2,695
		5,691	6,533
Creditors (amounts falling due within one year)	16a	(9,207)	(9,411)
<b>Net current liabilities</b>		<b>(3,516)</b>	<b>(2,878)</b>
<b>Total assets less current liabilities</b>		<b>496</b>	<b>1,118</b>
Creditors (amounts falling due after more than one year)	16a	(2,606)	(2,922)
Provisions for liabilities and charges	17	(1,657)	(1,553)
<b>Total net liabilities before pension liability</b>		<b>(3,767)</b>	<b>(3,357)</b>
Pension liabilities	17	(578)	(474)
<b>Total net liabilities</b>		<b>(4,345)</b>	<b>(3,831)</b>
<b>Taxpayers' equity:</b>			
General fund	18	(4,349)	(3,835)
Revaluation reserve	19	4	4
		<b>(4,345)</b>	<b>(3,831)</b>

*Alistair Buchanan*  
Accounting Officer  
25 April 2008

The notes on pages 31 to 49 form part of these accounts.

**Cash Flow Statement***For the year ended 31 March 2008 (£000s)*

	Note	<u>2007-08</u>	<u>2006-07</u>
Net cash outflow from operating activities	20a	(12)	(4,167)
Capital expenditure and financial investment	20c	(364)	(754)
Receipts due to the Consolidated Fund which are outside the scope of the Department's activities	8, 29	120,025	255,000
Payments of amounts due to the Consolidated Fund		(120,873)	(256,647)
Financing	20d	–	6,019
Decrease in cash in the period	20e	<u>(1,224)</u>	<u>(549)</u>

The notes on pages 31 to 49 form part of these accounts.

**Statement of Net Operating Costs by Departmental Aim and Objectives***For the year ended 31 March 2008 (£000s)***AIM: To protect consumers' interests, wherever possible by promoting effective competition and only where necessary through regulation.**

Objective	2007-08			2006-07		
	Gross	Income	Net total	Gross	Income	Net total
1. Creating and sustaining competition	12,763	(12,763)	–	10,940	(10,940)	–
2. Regulating networks effectively	17,033	(17,033)	–	17,976	(17,976)	–
3. Helping to protect the security of Britain's energy supplies	1,893	(1,893)	–	2,446	(2,446)	–
4. Providing a leading voice in Europe	1,893	(1,893)	–	2,015	(2,015)	–
5. Helping to achieve sustainable development	4,517	(3,822)	695	4,512	(3,866)	646
6. Helping tackle fuel poverty	1,357	(1,357)	–	1,288	(1,288)	–
7. Better regulation	451	(451)	–	331	(331)	–
<b>Net operating cost</b>	<b>39,907</b>	<b>(39,212)</b>	<b>695</b>	<b>39,508</b>	<b>(38,862)</b>	<b>646</b>

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

The notes on pages 31 to 49 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 2007-08 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.

#### 1.2 Tangible fixed assets and depreciation

As permitted by the 2007-08 FReM, tangible fixed assets are no longer revalued on an annual basis using indices. Depreciated historical cost is now used as a proxy for current value as this realistically reflects consumption of the asset. Revaluations would not cause a material difference to the carrying value of fixed assets.

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
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. During the year, costs in respect of the Fossil Fuel Levy were reclassified as administration. They had previously been classified as programme costs. The comparative data for 2006-07 is unchanged. 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 operating costs. The charge is calculated at the real rate set by HM Treasury, 3.5 per cent for 2007-08, 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. During 2007-08 the estimate structure was revised from two Request for Resources down to one in order to better reflect Ofgem's responsibilities for the administration of environmental programmes. Comparative data for 2006-07 shows the balances for the two RfRs, consolidated into one.

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 2008 shows a negative taxpayers equity of £4.345 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. 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 2008-09 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 FRM 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.

### 1.16 Assets belonging to third parties

Assets belonging to third parties (such as money held in relation to the Fossil Fuel Levy and the Renewables Obligation) are not recognised in the balance sheet since Ofgem has no beneficial interest in them.

## 2. Analysis of net resource outturn by function

	2007-08					Estimate		Restated
	Outturn					Net total	Net total outturn compared with Estimate	2006-07
	Admin.	Other current	Gross resource expenditure	A in A	Net total			
£000	£000	£000	£000	£000	£000	£000	£000	
<b>Request for Resources 1</b>								
<b>Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry, and expenditure in connection with environmental programmes</b>								
A Gas and Electricity Markets Authority:								
Administration	37,535	–	37,535	37,534	1	3	2	1
B Climate Change Levy and Renewable Energy Guarantees of Origin:								
Administration	694	–	694	–	694	700	6	645
C Energy Efficiency and other Environmental Schemes:								
Administration	1,678	–	1,678	1,678	–	–	–	–
<b>Resource outturn</b>	<b>39,907</b>	<b>–</b>	<b>39,907</b>	<b>39,212</b>	<b>695</b>	<b>703</b>	<b>8</b>	<b>646</b>

## Notes to the departmental resource accounts *(continued)*

### 3. Reconciliation of Outturn to net operating cost and against Administration Budget

#### 3(a) Reconciliation of net resource outturn to net operating cost

	Note	2007-08	2006-07
		£000	£000
Net Resource Outturn	2	695	646
Prior period adjustments		–	–
Non supply income (CFERs)	5	–	–
Non supply expenditure		–	–
<b>Net operating cost</b>		<b>695</b>	<b>646</b>

#### 3(b) Outturn against final Administration Budget

	Note	2007-08		2006-07	
		Budget	Outturn	Budget	Outturn
		£000	£000	£000	£000
Gross Administration Budget	2	40,186	39,907	39,620	39,453
Income allowable against the Administration Budget	2	(39,483)	(39,212)	(38,917)	(38,807)
Net outturn against the Administration Budget		<b>703</b>	<b>695</b>	<b>703</b>	<b>646</b>

### 4. Reconciliation of resources to cash requirement

	Note	Estimate	Outturn	Net total outturn compared with estimate: saving/ (excess)
		£000	£000	£000
<b>Resource Outturn</b>	2	<b>703</b>	<b>695</b>	<b>8</b>
Capital:				
• Acquisition of fixed assets	13	1,000	751	249
• Investments		–	–	–
Non-operating A-in-A:				
• Proceeds of fixed asset disposals	20b	(50)	–	(50)
Accruals adjustments:				
• Non-cash items	11	255	82	173
• Depreciation	11	(1,000)	(735)	(265)
• New provisions and adjustments to provisions	11	(5)	(604)	599
• Other non-cash items	11	(45)	(42)	(3)
• Movement in working capital		–	(322)	322
• Use of provision	17	991	551	440
Excess cash receipts surrenderable to the Consolidated Fund	5	–	–	–
<b>Net cash requirement</b>		<b>1,849</b>	<b>376</b>	<b>1,473</b>

New provisions and adjustments to provisions are higher than estimated due to a restructuring within the Networks division.

**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 2007-08		Outturn 2007-08	
		Income	Receipts	Income	Receipts
		£000	£000	£000	£000
Operating income and receipts- excess A in A	6	-	-	-	-
Other operating income and receipts not classified as A in A	6	-	-	-	-
		-	-	-	-
Non operating income and receipts not classified as A in A	8	-	-	25	25
Surplus supply surrenderable to the Consolidated Fund	16	-	-	1,471	1,471
Other amounts collectable on behalf of the Consolidated Fund	8	-	-	120,000	120,000
Excess cash surrenderable to the Consolidated Fund	4	-	-	-	-
<b>Total income payable to the Consolidated Fund</b>		-	-	<b>121,496</b>	<b>121,496</b>

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

	Note	2007-08	2006-07
		£000	£000
Operating Income	9	39,212	38,862
Income authorised to be appropriated in aid		(39,212)	(38,862)
<b>Operating Income payable to the Consolidated Fund</b>	5	-	-

**7. Non-operating income – Excess A in A**

	Note	2007-08	2006-07
		£000	£000
Proceeds on disposal of fixed assets	20b	-	-
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
Fines		25	25
Fossil Fuel Levy receipts	29	120,000	120,000
Other amounts collectable		120,025	120,025

## 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 2007-08, there was no operating income not classified as A in A.

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

	2007-08		2006-07	
	A in A £000	Income £000	A in A £000	Income £000
Administrative income:				
Fees and charges to external customers	34,806	34,806	34,783	34,783
Fees and charges to other departments	4,406	4,406	4,024	4,024
	<b>39,212</b>	<b>39,212</b>	<b>38,807</b>	<b>38,807</b>
Programme income:				
Fossil Fuel Levy	–	–	55	55
<b>Total</b>	<b>39,212</b>	<b>39,212</b>	<b>38,862</b>	<b>38,862</b>

#### 9.2 Operating income analysis

	2007-08			2006-07		
	Income £000	Full costs £000	(Deficit) £000	Income £000	Full costs £000	(Deficit) £000
Administration income						
Gas and Electricity:						
Licence fees (external)	34,700	35,395	(695)	34,783	35,429	(646)
Other	4,512	4,512	–	4,024	4,024	–
Subtotal	39,212	39,907	(695)	38,807	39,453	(646)
Programme income:						
Fossil Fuel Levy	–	–	–	55	55	–
	<b>39,212</b>	<b>39,907</b>	<b>(695)</b>	<b>38,862</b>	<b>39,508</b>	<b>(646)</b>

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.

During 2007-08, income in respect of administering the Fossil Fuel Levy was reclassified from programme to administration expenditure (Note 1.5).

Other income includes:	2007-08 £000	2006-07 £000
Department for Environment, Food and Rural Affairs (DEFRA)	4,076	3,659
Other departments	330	332
Miscellaneous	106	33
	<b>4,512</b>	<b>4,024</b>

Income from DEFRA includes income received in respect of Ofgem's Millbank building (£3,975,000), and secondment income.

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

	2007-08		2006-07	
	Permanently employed staff	Others	Total	Total
	£000	£000	£000	£000
Wages and salaries	13,633	674	14,307	13,761
Social security costs	1,311	–	1,311	1,267
Other pension costs	2,645	–	2,645	2,580
Other staff costs	935	–	935	1,002
<b>Total</b>	<b>18,524</b>	<b>674</b>	<b>19,198</b>	<b>18,610</b>
Less recoveries in respect of outward secondments	(142)	–	(142)	–
<b>Total net costs*</b>	<b>18,382</b>	<b>674</b>	<b>19,056</b>	<b>18,610</b>

\* 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](http://www.civilservice-pensions.gov.uk)).

For 2007-08, employers' contributions of £2,588,000 were payable to the PCSPS (2006-07 £2,551,000) at one of four rates in the range 17.1 per cent to 25.5 per cent (2006-07 17.1 to 25.5 per cent) of pensionable pay, based on salary bands. The contribution rates reflect benefits accruing during 2007-08 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 £54,184 (2006-07 £26,965) 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 £3,088 (2006-07 £2,138), 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 (2006-07 £0).

## Average number of persons employed

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

Objective	2007-08		2006-07	
	Permanently employed staff	Others	Total	Total
Creating and Sustaining competition	100	3	103	95
Regulating networks effectively	118	3	121	123
Helping to protect the security of Britain's energy supplies	13	–	13	18
Providing a leading voice in Europe	12	–	12	14
Helping to protect the environment	36	1	37	40
Helping tackle fuel poverty	12	–	12	13
Better regulation	4	–	4	3
<b>Total</b>	<b>295</b>	<b>7</b>	<b>302</b>	<b>306</b>

Notes to the departmental resource accounts *(continued)*

## 11. Other administration costs

	Note	<u>2007-08</u>	<u>2006-07</u>
		£000	£000
<b>Rental under operating leases:</b>			
Hire of office equipment		23	82
Other operating leases		5,683	5,547
		<u>5,706</u>	<u>5,629</u>
<b>Non-cash items (see below):</b>			
Auditors' remuneration and expenses*		42	44
Depreciation	13	735	764
Loss on disposal of fixed assets		–	4
Cost of capital charge		(140)	(204)
Diminution in value of fixed assets		–	89
		<u>637</u>	<u>697</u>
<b>Other expenditure:</b>			
Contractors		5,053	6,020
Other accommodation costs		3,325	2,885
Office supplies and services		930	982
Travel and subsistence		603	771
Contracted laboratory costs		652	737
Training		542	501
Recruitment		988	402
Telecoms		245	238
Media and Communications		225	222
Library Services		114	178
Hospitality		104	96
Other expenditure		923	788
		<u>13,704</u>	<u>13,820</u>
<b>Provisions (non-cash):</b>			
Provided in year	17	604	625
Provision not required written back	17	–	(1)
Unwinding of the discount	17	58	73
		<u>662</u>	<u>697</u>
Movement in provision		662	697
		<u>20,709</u>	<u>20,843</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>2007-08</u>	<u>2006-07</u>
	£000	£000
Non-cash costs (admin)	1,299	1,394
Less non-cash income	–	–
<b>Total non-cash transactions</b>	<u>1,299</u>	<u>1,394</u>

Notes to the departmental resource accounts *(continued)*

## 12. Net programme costs

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
Fossil Fuel Levy costs	–	55
Programme costs	–	<b>55</b>
Programme income	–	(55)
<b>Net programme costs</b>	<b>–</b>	<b>–</b>

During 2007-08, Fossil Fuel Levy costs previously classified as programme expenditure were reclassified as administration expenditure (See Note 1.5)

## 13. Tangible fixed assets

	Furniture	Office equipment	Information Technology	Leasehold works	Total
	£000	£000	£000	£000	£000
<b>Cost or valuation</b>					
At 1 April 2007	383	1,523	1,337	4,297	7,540
Additions	–	315	436	–	751
Disposals	(27)	(88)	(49)	–	(164)
<b>At 31 March 2008</b>	<b>356</b>	<b>1,750</b>	<b>1,724</b>	<b>4,297</b>	<b>8,127</b>
<b>Depreciation</b>					
At 1 April 2007	336	645	973	1,590	3,544
Charged in year	17	249	209	260	735
Disposals	(27)	(88)	(49)	–	(164)
<b>At 31 March 2008</b>	<b>326</b>	<b>806</b>	<b>1,133</b>	<b>1,850</b>	<b>4,115</b>
<b>Net book value</b>					
<b>At 31 March 2008</b>	<b>30</b>	<b>944</b>	<b>591</b>	<b>2,447</b>	<b>4,012</b>
<b>Net book value</b>					
<b>At 31 March 2007</b>	<b>47</b>	<b>878</b>	<b>364</b>	<b>2,707</b>	<b>3,996</b>
<b>Asset financing:</b>					
Net book value of owned assets at 31 March 2008	<b>30</b>	<b>944</b>	<b>591</b>	<b>2,447</b>	<b>4,012</b>

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

Notes to the departmental resource accounts *(continued)*

## 14. Debtors

## 14(a) Analysis by type

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
<b>Amounts falling due within one year:</b>		
Trade debtors	1,376	1,048
Accrued income	126	79
Prepayments	2,317	2,266
HM Revenue and Customs (VAT)	263	273
Staff debtors	138	172
<b>At 31 March</b>	<b>4,220</b>	<b>3,838</b>

Staff debtors include loans outstanding, of which £85,000 relates to season ticket loans for 83 employees; and £51,000 relates to housing advances in respect of 4 employees.

**Staff debtors due after more than one year:** The balance of £51,000 (2006-07: £78,000) relating to housing advances comprises £41,000 (2006-07: £66,000) which is repayable in instalments after one year.

## 14(b) Intra-government balances

	<b>2007-08</b>	<b>Restated 2006-07</b>
	£000	£000
Balances with other central government bodies	1,732	1,361
Balances with local authorities	813	781
Balances with public corporations and trading funds	–	–
Balances with bodies external to government	1,675	1,696
<b>Total debtors at 31 March</b>	<b>4,220</b>	<b>3,838</b>

## 15. Cash at bank and in hand

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
Balance at 1 April	2,695	3,244
Net change in cash balances	(1,224)	(549)
<b>Balance at 31 March</b>	<b>1,471</b>	<b>2,695</b>
The following balances at 31 March are held at:		
Office of HM Paymaster General	1,316	2,643
Commercial banks and cash in hand	155	52
<b>Balance at 31 March</b>	<b>1,471</b>	<b>2,695</b>

Notes to the departmental resource accounts *(continued)*

## 16. Creditors

## 16(a) Analysis by type

	<u>2007-08</u>	<u>2006-07</u>
	£000	£000
<b>Amounts falling due within one year:</b>		
Other Taxation and Social Security	474	434
Trade creditors	641	364
Staff creditors	2	5
Deferred licence fees	3,924	3,557
Leasehold reverse premium	316	316
Accruals and other deferred income	2,379	2,040
Amounts issued from the Consolidated Fund for supply but not spent at year end	1,471	2,695
Excess cash receipts	-	-
Consolidated Fund Extra Receipts due to be paid to the Consolidated Fund:		
received	-	-
receivable	-	-
<b>Balance at 31 March</b>	<b><u>9,207</u></b>	<b><u>9,411</u></b>
	<u>2007-08</u>	<u>2006-07</u>
	£000	£000
<b>Amounts falling due after more than one year:</b>		
Leasehold reverse premium	2,606	2,922
<b>Balance at 31 March</b>	<b><u>2,606</u></b>	<b><u>2,922</u></b>

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 £2.922 million 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	
	<u>2007-08</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2006-07</u>
	£000	£000	£000	£000
Balances with other central government bodies	2,811	4,327	-	-
Balances with local authorities	-	-	-	-
Balances with public corporations and trading funds	-	-	-	-
Balances with bodies external to government	6,396	5,084	2,606	2,922
<b>Total creditors at 31 March</b>	<b><u>9,207</u></b>	<b><u>9,411</u></b>	<b><u>2,606</u></b>	<b><u>2,922</u></b>

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

	Early Retirement
	£000
Balance at 1 April 2007	<b>1,553</b>
Provided in the year	583
Unwinding of the discount	58
Provisions not required written back	–
Provision utilised in the year	(537)
Net movement in year	104
<b>Balance at 31 March 2008</b>	<b>1,657</b>

The total movement in provision in 2007-08 was an increase of £104,000.

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 £1,817,592.

**Pension liabilities**

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
<b>Provision at 1 April 2007</b>	<b>474</b>	<b>407</b>
Interest cost	21	22
Actual benefit payments	(14)	(14)
Actuarial loss	97	59
<b>Provision at 31 March 2008</b>	<b>578</b>	<b>474</b>
Net movement in year (excluding actuarial loss)	7	8

**History of experience losses**

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
Experience losses/(gains) arising on the scheme liabilities	107	(6)
Amount recognised as a percentage of present value of scheme liabilities	18.5%	(1.2%)
Total amount recognised in statement of recognised gains and losses	97	59
Percentage of present value of the scheme liabilities	16.8%	12.5%

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 2008. The major assumptions used by the actuary were:

	At 31 March 2008 % (per annum)	At 31 March 2007 % (per annum)
Inflation assumption	2.75	2.75
Rate of increase in salaries	4.3	4.3
Investment return in excess of price increases	2.5	1.8
Rate of increase for pensions in payment and deferred income	2.75	2.75

### Analysis of Actuarial Loss

	<b>2007-08</b>	<b>2006-07</b>	<b>2005-06</b>
	£000	£000	£000
Changes in assumptions underlying the present value of scheme liabilities	(10)	65	–
Experience (gains)/losses arising on the scheme liabilities	107	(6)	31
Per statement of recognised gains and losses	97	59	31

From 31 March 2008, the discount rate for pension scheme liabilities changed from 1.8 per cent to 2.5 per cent. This rate is reflected in the valuation of the pension scheme liability as at 31 March 2008.

## 18. General Fund

	<b>2007-08</b>		<b>2006-07</b>	
	£000	£000	£000	£000
<b>Balance at 1 April</b>		<b>(3,835)</b>		<b>(7,899)</b>
Net Parliamentary Funding:				
Draw Down	–		6,019	
Deemed Supply	1,847		1,597	
		1,847		7,616
Net transfer from operating activities:				
Net operating cost		(695)		(646)
Surplus supply repayable to the Consolidated Fund		(1,471)		(2,695)
Non-cash charges:				
Cost of capital	(140)		(204)	
Auditor's remuneration	42		44	
		(98)		(160)
Realised on revaluations and disposals of assets		–		8
Losses relating to pension liabilities		(97)		(59)
<b>Balance at 31 March</b>		<b>(4,349)</b>		<b>(3,835)</b>

## 19. Revaluation Reserve

	<b>2007-08</b>	<b>2006-07</b>
	£000	£000
Balance at 1 April	4	31
Arising on revaluation during the year (net)	–	(19)
Transferred to General Fund in respect of realised element of the Revaluation Reserve	–	(8)
<b>Balance at 31 March</b>	<b>4</b>	<b>4</b>

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>2007-08</u>	<u>2006-07</u>
	Note	£000	£000
<b>Net operating cost</b>	3a	695	646
Adjustments for non-cash transactions	11	(1,299)	(1,394)
Increase in Debtors	14a	382	1,246
<i>Less movements in debtors relating to items not passing through the OCS</i>	14a	–	–
Decrease in Creditors	16a	204	3,401
<i>Less movements in creditors relating to items not passing through the OCS</i>	16a	(837)	(544)
Decrease in long term creditors	16a	316	317
Use of provisions	17	551	495
<b>Net cash outflow from operating activities</b>		<u><b>12</b></u>	<u><b>4,167</b></u>

## 20(b) Analysis of capital expenditure and financial investment

		<u>2007-08</u>	<u>2006-07</u>
	Note	£000	£000
Tangible fixed asset additions	20c	364	754
Proceeds on disposal of fixed assets	20c	–	–
<b>Net cash outflow from investing activities</b>		<u><b>364</b></u>	<u><b>754</b></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
<b>Request for Resources 1</b>				
Protecting consumers by regulating monopolies and promoting competition in the electricity and gas industry, and expenditure in connection with environmental programmes (Note 13)	751	–	–	751
Change in creditors	(387)	–	–	(387)
<b>Total 2007-08</b>	<u><b>364</b></u>	<u><b>–</b></u>	<u><b>–</b></u>	<u><b>364</b></u>
<b>Total 2006-07</b>	<u><b>754</b></u>	<u><b>–</b></u>	<u><b>–</b></u>	<u><b>754</b></u>

## 20(d) Analysis of financing

		<u>2007-08</u>	<u>2006-07</u>
	Note	£000	£000
From the Consolidated Fund (Supply) – current year	18	–	6,019
Advances from the Contingency Fund		10,000	10,000
Repayments to the Contingency Fund		(10,000)	(10,000)
<b>Net financing</b>		<u><b>–</b></u>	<u><b>6,019</b></u>

**20(e) Reconciliation of Net Cash Requirement to change in cash**

		<u>2007-08</u>	<u>2006-07</u>
	Note	£000	£000
Net cash requirement		(376)	(4,921)
From the Consolidated Fund (Supply) – current year	20d	–	6,019
From the Consolidated Fund (Supply) – prior year	20d	–	–
Amounts paid over to the Consolidated Fund – received in prior year		(848)	(1,647)
Excess cash surrenderable to the Consolidated Fund		–	–
Amounts due to the Consolidated Fund received and not paid over		–	–
Decrease in cash		<u>(1,224)</u>	<u>(549)</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>2007-08</u>	<u>2006-07</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>2007-08</u>	<u>2006-07</u>
	£000	£000
<b>Obligation under operating leases comprise:</b>		
Land and buildings:		
Expiry within 1 year	–	–
Expiry after 1 year but not more than 5 years	99	99
Expiry thereafter	5,828	5,704
	<u>5,927</u>	<u>5,803</u>
Other:		
Expiry within 1 year	1	11
Expiry after 1 year but not more than 5 years	2	7
Expiry thereafter	–	–
	<u>3</u>	<u>18</u>

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**24. Other financial commitments**

Ofgem had not entered into any non-cancellable contracts (which are not operating leases) as at 31 March 2008.

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**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 2008 there were no contingent liabilities requiring disclosure.

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**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 2008.

## 27. Related Party Transactions

Ofgem transferred £10.783 million to BERR 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 Utility Regulation. Income received in year was £4.1m from DEFRA, £66k from Postcomm, £136k from NI Authority for Utility Regulation and £123k from BERR.

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.

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## 28. Post balance sheet events

There were no reportable post balance sheet events between the balance sheet date, and the 30 April 2008, the date when the Accounting Officer despatched the accounts to HM Treasury. The financial statements do not reflect events after this date.

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## 29. Third Party Assets

### *Fossil Fuel Levy*

Ofgem is responsible for setting, collecting and administering the Fossil Fuel Levy (FFL) via commercial bank accounts. BERR 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 Business, Enterprise and Regulatory Reform 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 21 September 2007 and 20 March 2008, £55 million and £65 million respectively, were transferred to the Consolidated Fund from the England and Wales account on this basis.

The balance held at 31 March 2008 in the England and Wales account was £30 million and the Scotland account held £106 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 Managing Public Money 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.

*Renewables Obligation*

Under the Renewables Obligation Order 2006, Ofgem on behalf of the Secretary of State for Business, Enterprise and Regulatory Reform is responsible for administering the Renewables Obligation. The Renewables Obligation requires suppliers to source a certain portion of the electricity they supply from renewable sources. Alternatively, suppliers can buy out of the obligation.

Buyout payments for a particular compliance period are redistributed to suppliers by 1 November following the end of the compliance period (which runs from April to March each year). The balance on the Renewables Obligation account at year-end is normally zero.

In 2007, a supplier wished to cancel their supply licence. To enable them to do this they were required to meet their licence conditions, which included complying with the Renewables Obligation. The supplier made a total payment of £978,000 in 2007-08 in order to buy out this Obligation early. This amount, plus interest accrued, is the amount which is held in the England and Wales Renewables Obligation account as at 31 March 2008.

The balance on the Renewables Obligation account as at 31 March 2008 (£999,000), together with other supplier buyout payments received post year-end, will be redistributed to suppliers by 1 November 2008.











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