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Adanma Joseph-Anyaegbu
Ofgem
9 Millbank
London
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17 December 2015

Dear Adanma,

RIIO Accounts: Consultation on proposed regulatory financial reporting framework

This letter sets out our response on behalf of National Grid Electricity Transmission plc (NGET) and National Grid Gas plc (NGG) - herein known as National Grid - to Ofgem's consultation issued on 4th November 2015 for a new regulatory reporting framework.

We remain very supportive of the concept of RIIO accounts and the need to report performance on a basis more consistent with the RIIO regulatory approach. We welcome the developments made since the initial consultation in June and the inclusion of appendix 2 in this consultation of an example of what RIIO accounts may look like. We are further encouraged with the issuing of the draft RIIO accounts support module (RASM) on 3rd December and the planned teleconference and workshop to review this in more detail, both of which we will be attending. We await the issuing of a similar RASM for our Transmission businesses.

The inclusion in the consultation document of the responses to the initial consultation and your consideration of these responses allows us to see that you are taking the thoughts of the NWO's into account as the project develops. This is especially true of the proposed change to the reporting deadline of issuing RIIO accounts from July to September. We were also pleased to see clarification that RIIO accounts are to be prepared at a company level. We still believe the most significant question is the timing for the implementation of the new RIIO accounts and whether the first set of RIIO accounts are required for the year ending March 2017.

This implementation date and the form of changes to licence modifications is the main focus of this consultation. We have included a more detailed response to this question but our primary comments are as follows:

- We believe network operating companies (NWOs) should be fully involved in the decision on which year to implement RIIO Accounts under all the possibilities presented in the consultation
- NWOs should have, as a minimum, the option to defer implementation beyond the 2016/17 reporting year by giving notice to the Authority

Given the above, the licence modifications should not be unduly rushed through.

We believe the implementation of RIIO accounts will add to the regulatory burden on NWOs as they will have to amend processes and generate financial information from different sources, and on a basis that is substantially different, to their IFRS or UKGAAP financial statements. In addition, current RIGS and RRP requirements require information on the same basis as the current regulatory accounts and if these requirements are not removed, the regulatory burden will be increased even further.

As we have previously noted we remain supportive of the concepts. We have experience of reporting IFRS financial results and of voluntarily disclosing additional information on our regulatory performance and position as part of reporting our annual results. We are keen to use this experience to progress the development of the regulatory financial reporting standard (RFRS) and will continue to work closely with Ofgem.

If the RFRS has been developed to a sufficient level, we plan on using our 2015/16 data to help identify issues that we may encounter in producing audited accounts. We plan to engage our auditors in this process and would be happy to discuss our experiences to further develop the RFRS framework.

We have provided our detailed responses to all the questions in the consultation in the appendix to this response in the format requested.

This response is not confidential.

Yours sincerely

By email

Richard Allman

Appendix - FEEDBACK QUESTIONNAIRE

Section 1 - About you	
Your name	Richard Allman
Job title	Financial Controller, RIIO Optimisation
Contact details	01926 656354 Richard.allman@nationalgrid.com
Organisation name	National Grid, including National Grid Electricity Transmission plc and National Grid Gas plc
Please state whether your response is confidential or not	Not confidential

Questions	Response
Chapter 1 – Concept and content of RIIO accounts	
<p>1. Do you have any comments on the form and content of RIIO accounts illustrated in appendix 2?</p>	<p>The inclusion of the appendix is helpful to allow people to understand the concepts being proposed. However, without a full set of RFRS and the associated guidance, it is difficult to provide a complete response. The appendix also left us with a number of unanswered questions and concerns on specific areas (e.g. tax disclosures, pension disclosures, materiality etc.). These queries may get resolved once the formal consultation on the RFRS is issued, but equally we are happy to provide our list of questions and points to note / clarify earlier if this would be helpful.</p> <p>The consultation is helpful in confirming that only one set of accounts is required at a company level. The presentation material from the investor community event indicated that segmental disclosures would be provided, but the consultation does not explain to what level this information will be required. We have some concern that this may lead to the principal statements having to be prepared for each licence / network which would add to the regulatory burden and complexity of the RIIO accounts.</p>

	<p>Care needs to be taken not to create too great a reporting burden. An appropriate balance needs to be set between the additional costs of preparing the RIIO Accounts and the customer benefit they will provide.</p> <p>The true test will be in applying the RFRS and RASM to real data, something we would be keen to do using 2015-16 results despite the additional burden this will place on us. We will use this opportunity to engage with our auditors and Ofgem to help further develop the reporting framework in advance of its full implementation.</p>
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Chapter 2 – Timetable and licence modifications

<p>2. Do you agree that the four implementation planning options set out in this chapter would allow for necessary flexibility in the timetable for implementing RIIO accounts? If not, please suggest an alternative option.</p>	<p>The options do potentially provide the necessary flexibility. That said, we believe the NWOs should be fully involved in the decision on which year to implement the RIIO Accounts. Any representations made, and the Authority’s response to such representations, should be made available to all NWOs in advance of the 31 October 2016 date proposed in the draft licence condition.</p> <p>We also need to understand the expectations when preparing the first set of RIIO accounts to be published e.g. the process on how auditors will get “comfortable” with opening balances and whether there is a need to have prior period comparatives included and audited.</p>
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<p>3. Out of the four proposed implementation planning options we set out, which do you consider to be achievable and desirable?</p>	<p>We refer to the consultation (para 2.5), where it is acknowledged, from your own experience to date and also the concerns expressed as part of the initial consultation, that timelines need to be extended as there is still a substantial amount of work to do to develop RIIO accounts from both a technical and</p>
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practical level.

We welcome the recognition that the work to get the 'fairly presents' audit opinion cannot be underestimated and your engagement with the audit profession is continuing.

We are pleased to see the publication of a draft RASM for the GD business and the planned workshop in January 2016 to review the model in detail with NWOs and the creation of a change log thereafter. We still await the draft RASM for what we consider the more complicated Transmission businesses.

For the above reasons (including the points raised in question 2), the timetable should not be unduly rushed, and a provision to enable a later implementation date at this stage is appropriate.

We welcome that option ii gives NWOs the option to elect to defer implementation from 2016/17 and consider that the same option should be available in option iii. Applying RIIO accounts will be more complex for some NWOs than others and they, or their auditors, may not believe they could deliver a quality, audited set of accounts for 2016/17 by the licence due date. Such a decision would not be taken lightly by the NWO due to the potential risk of reputational damage if they are in the minority. Equally there may be company specific reasons why deferring implementation by a year may be in both the company's and consumers interests e.g. National Grid is changing its auditors for the year commencing 1 April 2017. An audit of 2016/17 accounts would lead to 'set up and familiarisation costs' being incurred twice rather than just the once, which is not in the best interest of consumers.

	<p>For the above reasons we prefer options ii (company can elect to defer to 2017/18 providing its reasons to the Authority) and iv (deferral to 2017/18). Equally, option iii would be acceptable if the NWOs option to defer is added.</p> <p>As we noted earlier in our response to question 1, we intend to use 2015/16 to help identify and address the issues we may encounter in producing audited accounts and expect to engage with our auditors as part of this process.</p>
<p>4. Do you have any comments on the draft licence condition set out in appendix 3?</p>	<p>Our comments on Part A are included in our comments to questions 2 and 3.</p> <p>On Part B, we welcome the decision to adopt a 30 September publication date. However, we question the need for the publication to be in a CSV file when almost all other annual accounts and the current regulatory accounts are in PDF format.</p> <p>On Part C, we question the need to prepare a cash flow statement. This is not in the draft RASM which has been published; has not been included in previous discussions on concepts; is not included in appendix 2 (illustrative example); nor is it referred to elsewhere in the documentation. A full cash flow is included in the annual accounts for the company so this would be duplication. Inclusion of a movement in net debt table, in our opinion, is sufficient.</p> <p>On Part E, given the reliance on RFRS and the RASM to support preparation of the RIIO accounts, we believe any modifications need to be issued before the start of the financial year to which the changes relate. This is so NWOs and auditors are clear at the start of the year, the basis for preparation of the accounts. This should be the enduring</p>

	<p>principle that is reflected in the licence modification and is consistent with how changes to accounting standards are implemented.</p> <p>We consider that both the RASM and RFRS are likely to be developed on an iterative process in the short term and the current proposed 28 day notice of any changes would be more acceptable during this period rather than on an enduring basis.</p> <p>On Part G, we welcome Ofgem taking the opportunity to remove redundant AUPs. It would be better to include the remaining requirement in a separate condition. This may help to increase flexibility over the timetable for RIIO Accounts implementation.</p>
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Chapter 3 – The Regulatory Financial Reporting Standard

<p>5. Do you agree that the high level principles and prescribed regulatory framework set out in chapter 3 mean that RIIO accounts can be prepared on a 'fairly presents' basis?</p>	<p>We support a principles based approach to the RFRS and believe accounts are more likely to fairly present performance than with a rules based RFRS.</p> <p>We consider the audit profession need to comment on how a principles based approach can be developed to support a 'fairly presents' opinion.</p> <p>We would welcome the views of the Institute of Chartered Accountants in Scotland (ICAS) being sought as well as the ICAEW.</p>
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Chapter 5 – Reporting on regulatory corporate governance

<p>6. Do you have further comments on the revised draft regulatory corporate governance principles?</p>	<p>We welcome a 'principles' based approach and clarification that companies do not have to implement the Code itself.</p> <p>We assume that the additional principle in RC5 is the revised Code's requirement to prepare a viability statement and highlight how price control arrangements</p>
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and ring fence conditions play their part. We would like this confirming with further guidance.

On RC4, we feel more guidance is required to understand if the intention is to explain how directors are minimising the pension costs funded by consumers as the independent pension trustees are responsible for the governance of the schemes for the interests of the scheme membership and not the company.

Chapter 6 – Impact assessment

7. Do you agree with our assessment of the possible impacts?

We do not agree the regulatory burden will not increase. The current regulatory accounts are based on accounting standards and consistent with statutory accounts making their production and audit costs relatively low. RIIO Accounts will be on a fundamentally different framework, will be more expensive to produce and are likely to be more expensive to audit as a result of unfamiliarity by the audit firms. We also wonder if this will reduce the ability of mid-tier firms to compete for audit work, thus reducing competition.

As we noted in our response to question 1, we are concerned that the level of segmental disclosures and proposed reconciliations will add to the complexity and burden in preparing the RIIO accounts.

Ofgem's impact assessment indicates that other regulatory reporting **may be** reduced in future. The current RIGS and certain RRP table requirements include reporting IFRS data akin to the current regulatory accounts. The current consultation does not propose to remove that reporting which means the RIIO Accounts represent additional obligations without removing the need to prepare form of control specific IFRS accounts.

	<p>These parts of the RIGS / RRP requirements should be removed. We also note that Ofgem believe the RIIO Accounts will improve understanding of risk levels and allow a lower cost of capital. We agree that the RIIO Accounts may make risk more transparent. There is a risk that investor perception of risk increases with RIIO Accounts.</p>
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ANY OTHER COMMENTS

<p>8. Please use this section to let us know of any other thoughts you might have on the further development of RIIO accounts.</p>	<p>We believe the project is progressing, as evidenced by issuing a draft RASM and the illustrative example of the RIIO accounts provided in this consultation.</p> <p>We can see that Ofgem are responding positively to the feedback received from NWOs most noticeably on the timetable and making this the primary focus of this consultation. We also welcome the engagement with the audit profession in developing the standalone RFRS and the engagement over the 'fairly presents' opinion.</p> <p>There is still much work to be done to progress the RFRS and issue guidance which will enable National Grid to use 2015/16 to 'trial' the production of RIIO accounts to help identify and address issues, engaging with our auditors as part of the process.</p> <p>If investor responses to the consultation are pushing for regulatory performance information on an earlier timescale than the project may deliver, it may be worth considering asking networks to add additional disclosures akin to the statements of regulatory performance and financial position, returns and perhaps some key reconciliations within their annual published accounts rather than preparing separately audited RIIO accounts.</p>
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