

## **GEL Financial Framework**

Treasury & Resources Department and Commerce & Employment Department representatives consider that the approach set out below provides an interim and pragmatic framework for the forthcoming price determination:

1. T&R requires GEL to be run on the basis of building up cash reserves to fund CAPEX;
2. As part of future price controls T&R and GEL will propose a level of cash reserves considered appropriate for GEL's business needs based on objective criteria, in particular efficiency considerations\*;
3. T&R will determine the level of returns it requires as shareholder expressed as a % of the cash reserve (or the returns generated from the cash reserve) each year\*\*;
4. Based on the levels of cash reserves maintained over recent years and current States Guidance (see below), T&R does not anticipate that the level of returns required would exceed £0.5m in any one year;
5. T&R will not require a dividend based on the value of tangible assets but insists that, for accounting purposes, the value of those assets should continue to be based on historic costs and appropriate depreciation policies as at present;
6. T&R recognises that the above approach will result in an accounting loss being recorded for some years, and an accounting profit for other years. Over 10 years (roughly a full CAPEX cycle for GEL) the accumulated profits/losses, returns to shareholder, change in cash reserves and any tax paid should balance out;
7. This mix of profits and losses is acceptable whilst shareholder value is maintained and T&R will publicly promote this principle;
8. The financial framework within which GEL is required to operate will be taken into account by the OUR but the actual levels of OPEX and CAPEX that are used for the price determination will be subject to the usual statutory processes involving GEL and the OUR, with the ultimate options of mediation or a formal appeal to resolve any disputes.

The effects of adopting this interim approach can be reviewed near the end of the forthcoming price determination period and, if necessary, revised for future determinations

\* A logical basis for calculating the return rather than just stipulating an arbitrary sum will be necessary in order to achieve a defensible position should any interested third party appeal a price determination.

\*\*Consideration will need to be given as to how the returns may be paid to T&R within the current GEL Mem. & Arts. and Guernsey Company Law.

### **States Guidance on shareholder returns:**

*“Financial performance targets for Guernsey Electricity Limited shall be set so as to deliver improved efficiency in fulfilling the requirements of the Public Supply Obligation imposed under the regulatory regime whilst drawing a balance between seeking a commercial return on the resources employed and the effect on the community of any increase in charges which may result”*

GS

16 March 2006