

Overview

The Directors consider that during the year the Company has been in compliance with the requirements set out in Section 1 of the Combined Code incorporating the principles of good governance and code of best practice (the "Combined Code"). The Company intends to comply with the provisions of the revised Combined Code published in July 2003 which will apply to the Company in the year ending 31 March 2005.

The Board

Adrian Montague held office as Chairman and Mike Alexander served as Chief Executive, throughout the year. The other Executive Directors are David Gilchrist, Managing Director Generation, and Martin Gatto, who was appointed Interim Finance Director following the resignation of Keith Lough on 8 December 2003. In addition there are six further Non-Executive Directors. Biographies of the Directors are set out on pages 28 and 29. The Chief Executive is responsible for safety throughout the Group.

The Directors are satisfied that the Company also complies with the sections of the Combined Code concerning the balance of the Board. Throughout the year, the number of Non-Executive Directors (including the Chairman) was greater than the number of Executive Directors. At the start of the year the Company had three Executive and four Non-Executive Directors in addition to the Chairman. At the year end the Company had three Executive and six Non-Executive Directors in addition to the Chairman. With the exception of Adrian Montague, who held an executive office temporarily for part of the previous financial year (following his appointment as Executive Chairman in November 2002), all Non-Executive Directors are independent. The Company's independent Non-Executive Directors are currently Clare Spottiswoode, William Coley, Pascal Colombani, John Delucca, Ian Harley and Sir Robert Walmsley. Clare Spottiswoode was the Company's Senior Non-Executive Director and Deputy Chairman throughout the year. During the year Sir Robert Hill retired and Duncan Hawthorne resigned as Non-Executive Directors. The Remuneration Committee Report on pages 36 to 42 provides further details of appointments to and resignations from the Board during the year.

At each Annual General Meeting any Director who has been appointed by the Board since the previous Annual General Meeting is required to retire and may seek election, together with such other Directors so as to ensure that at least one third of the Directors for the time being stand for election or re-election. In order to comply with the provisions of Rule A.6 of the Combined Code, all Directors are required to seek re-election at least every three years. The Company's policy is that Directors should retire at the first Annual General Meeting after their 65th birthday. Exceptions to the policy may be made from time to time to ensure an orderly transition in the membership of the Board.

The Board meets sufficiently regularly to discharge its duties effectively and at least 11 times in any year. It met 18 times during the year ended 31 March 2004. There is frequent contact amongst the Directors between Board Meetings to progress the Company's business.

All of the Non-Executive Directors serving on the Board have held senior positions in other major organisations either in the UK or internationally. Each of them is involved in decision making on key issues facing the Group and brings a wide range of experience to the Board. The Non-Executive Directors of the Company meet as a group from time to time without Executive Directors present and from time to time also meet without the Chairman present.

In accordance with the requirements of the Combined Code, the Board has a number of matters reserved to it, including appropriate strategic, financial and organisational matters. These are considered at the Board's monthly meetings. The Board receives reports covering operational, financial, safety, risk management and regulatory performance to assist it in identifying key issues for the business on a regular and timely basis. All Directors may obtain independent professional advice at the Company's expense and all Directors have access to the advice and services of the Company Secretary who is accountable to the Board through the Chairman on all corporate governance matters. Where appropriate, matters have been delegated to Board Committees, all of which have written constitutions and terms of reference. Individual Directors, their roles and membership of the various committees are identified on pages 28 to 29 of the Annual Report.

Risk Management

The Board is responsible for determining strategies and policies for risk and control and management is responsible for designing, operating and monitoring risk and control processes which implement Board policies effectively. In accordance with the Turnbull Guidance, risk management and internal control are considered by the Board and its Committees on a regular basis during the year.

The risk management process operating throughout the financial year was based on the identification, mitigation and monitoring of the key risks that influence the Company's strategy and business objectives. In light of the Company's decision to seek Government support in September 2002, and in view of the disposal of British Energy's international interests and its concentration on its UK operations, the Board agreed steps in April 2003 to review its risk management and corporate governance procedures and committee structure. Further details of the Group's committee structure appear below.

At its regular meetings, the Board reviews the Group's business objectives and the risks and controls associated with these business objectives. Specific categories of risk are also reviewed by appropriate committees, including the Group Risk Management Committee (GRMC) and subsidiary boards. Risks reviewed by the Board include: safe operation of our plant; operational risks including reliability, output, plant condition and human performance; the financial position of the Group; risks relating to the current Group restructuring; changes in energy markets; nuclear safety and safety regulations; commercial and environmental regulation; policy proposals by legislative bodies in the markets in which we operate; treasury and trading financial exposures; major contracts; and the acquisition of radioactive waste management services.

Throughout the year the Company's reporting arrangements operated across the Group's operating subsidiaries and corporate functions, monitoring business performance against key performance indicators and the business plan. Risk logs identifying business risks facing the Group as a whole and particular parts of the business were regularly considered at subsidiary and divisional level and reported to the Group's executive and mitigation plans were established and monitored. The Group's principal operating subsidiaries monitored internal control and risk mitigation throughout the year. In particular the Generation Boards (the boards of the UK nuclear subsidiaries) reviewed the operation of British Energy's UK nuclear fleet and risk and internal control issues affecting those businesses. The separate arrangements which operated for AmerGen are described below.

The conduct of risk assessment involves senior management of all of the Group's business units in addition to the Executive Directors. The results of these assessments are summarised and reported to the Board. These risk assessments will continue to be used as part of the Company's evaluation of the risks it faces.

The Board also received regular reports on risks associated with AmerGen (the United States joint venture with Exelon in which the Company held a 50% interest) prior to the disposal of our interest in December 2003. During the period of ownership of the Company's interest in AmerGen its operation was integrated with the Exelon group. Its risk management processes were separate from those applying within British Energy. British Energy appointed its own Financial Manager for AmerGen and chaired the AmerGen Finance Sub-Committee (which oversaw the operation of financial controls at AmerGen and had a similar role to the Company's Audit Committee) at its meetings throughout the year.

Committee Structure During the Year Ended 31 March 2004

Early in the year, the Company undertook a review of its committee structure. In the period subsequent to the events of September 2002, the Board had increasingly adopted a management role in the Group's business necessitated by the complex issues facing British Energy. These arrangements were reviewed following the appointment of Mike Alexander as Chief Executive. The new structure allows the Board to focus to a greater extent on strategy and review of business risks and to delegate the management of the business to the executive.

It is the Company's policy that committees are provided with sufficient resources to undertake their duties. The Company may make further changes in due course in order to comply with further developments in corporate governance best practice. The current terms of reference for each committee is available on the Company's website.

Board Committees

The current committee structure is described below:

Audit Committee

The Audit Committee is comprised entirely of independent Non-Executive Directors and was chaired by Ian Harley throughout the year. John DeLuca was appointed as Deputy Chairman of the Committee in April 2004. Ian Harley and John DeLuca are considered to be the financial experts on the Audit Committee. The Audit Committee has the primary purpose of assisting the Board in overseeing the integrity of the Company's financial statements, and overseeing the Company's compliance with legal and regulatory requirements. The Committee is also responsible for considering and recommending appropriate accounting policies for the Group, and reviewing the adequacy and effectiveness of internal control and compliance procedures within British Energy and ensuring that the Group complies with all statutory requirements in relation to the principles, policies and practices adopted in the preparation of the financial statements. The Committee reviewed risk management processes across the Group including actions to mitigate or control key risks facing British Energy. The Committee receives reports from both external and internal auditors in relation to matters arising from their work and is also responsible for encouraging and monitoring the adoption of best practice in corporate governance. The Committee receives reports twice per annum from the GRMC. The Committee reviews the scope and results of the external audit including the auditors' cost effectiveness, independence and objectivity, and is responsible for making recommendations to the Board in relation to the appointment and independence of the external auditors and their remuneration. The Committee also reviews the nature and extent of the non-audit services provided by the external auditors to the Group to ensure that these are appropriate, and that a balance of objectivity and value for money is maintained. Six meetings of the Audit Committee were held during the year.

Remuneration Committee

A separate Remuneration Report containing details of the Remuneration Committee appears on pages 36 to 42.

Nominations Committee

Throughout the year the Nominations Committee was comprised entirely of Non-Executive Directors and was chaired by Adrian Montague. The Committee advises the Board in relation to senior appointments throughout the Group. Board appointments recommended by the Nominations Committee are made after an appropriate search and selection process has been undertaken, including, where appropriate the use of external advisers to identify suitable candidates. The Nominations Committee met four times during the year.

Safety, Health and Environment Committee

This Committee provides advice to the Board in relation to the health and safety of staff, contractors, visitors and the general public, plant safety and the environmental performance of British Energy. It reviews key safety and environmental risks affecting British Energy's business and the actions taken to mitigate or control them. It is chaired by Sir Robert Walmsley (who succeeded Sir Robert Hill who retired in July 2003) and also includes three independent experts as well as the Managing Director Generation and certain other Directors and senior managers of the Group. The meetings, which consider both site specific and generic issues, are held in rotation at the nuclear power stations with the Station Manager and site safety representatives in attendance. The Committee met four times during the year.

Nuclear Performance Review Committee

The Nuclear Performance Review Committee first met in November 2003. Its role is to consider and advise the Board and the Executive on issues relating to the performance of and improvements to the Group's UK nuclear fleet including plant reliability, preventive maintenance and Materiel Condition. The Committee has focused on the implementation and direction of the Company's ongoing Performance Improvement Programme. The Committee is chaired by William Coley and its membership includes the Chief Executive, other Non-Executive Directors with appropriate technical expertise, the Managing Director Generation and certain other senior managers with appropriate technical expertise. The Committee met three times during the year and it is intended that henceforth it will meet at least four times a year.

Executive Committee

In April 2003, the Company formed a new Executive Committee through which the Chief Executive, with the assistance of a number of senior executive colleagues, directs the business of the Group in accordance with delegated authorities from the main Board. The Executive Committee meets weekly to maintain close scrutiny and management of the Company's affairs, directing performance, taking corrective action and ensuring the Board is kept abreast of all material events.

Subsidiary Boards

Throughout the year a number of executive management committees and subsidiary boards were used to assist the Directors in controlling the business. These included the Boards of British Energy's two nuclear generation subsidiaries which hold nuclear site licences (the Generation Boards) which directed operational and safety policy in the Group's nuclear operations. The Chief Executive and executives on the Generation Boards continue to direct the operational and safety policy of our UK nuclear operations.

Group Risk Management Committee

The GRMC is an executive committee chaired by the Chief Executive. The GRMC meets every two months to review the group-wide risk management processes of the business, maintain an overview of the risks facing the business and reports to the Audit Committee on a regular basis. The Committee met eight times during the year. The Trading Risk Sub-Committee reports to the GRMC.

Trading Risk Sub-Committee

This is a Sub-Committee of the GRMC. It is chaired by the Interim Finance Director. The Sub-Committee meets at least quarterly to review the risks, controls and limits of the Company's trading activity. It also considers and recommends improvements and developments to the controls in place to govern trading activities and considers extensions to those trading activities, in advance of approval being sought from either the Board or the Executive Committee. The Sub-Committee met four times during the year.

Pensions Committee

This is an executive committee which monitors the management of the two Group Pension Schemes and is chaired by Sally Smedley, the Group's Human Resources Director. The Chairmen of the British Energy Generation Group Trustees and the British Energy Combined Group Trustees are members, as are certain other Directors and senior managers of the Group. The Committee reviews and advises on the policies being adopted by the Trustees of these Schemes and is responsible for advising the Board on all matters relating to these Schemes. The Committee met twice during the year and focused particularly on preparing proposals to address the expected pension fund deficits following the results of the triennial actuarial valuation as at 31 March 2004.

Disclosure Committee

This Committee was established by the Company as part of its response to the requirements of the United States Sarbanes-Oxley Act of 2002. It is intended that the Committee will be chaired by the Group Financial Controller, and comprises management level representatives of operational and corporate departments from throughout the Group. Its role is to review the accuracy and completeness of the Company's proposed financial and certain other public statements and/or reports. The Committee met eight times during the year. It reports to the Audit Committee and the Chief Executive and Interim Finance Director.

Organisational Structure

There are clearly defined lines of accountability throughout the Group. These include strict authorisation approval and control procedures within which senior management operate. Similarly the senior management team within each subsidiary or division is responsible for its internal financial controls. Those management teams operate within an overall framework determined by the Board.

Investment Approval

The approval of capital and revenue schemes above certain limits is reserved to the Board. Other investment decisions are delegated for approval in accordance with authority limits. The Group has comprehensive appraisal and monitoring procedures which apply to all material investment decisions.

Business Planning

A comprehensive business planning and budgeting process to establish plans and targets, against which performance is regularly monitored, is undertaken each year. Key business risks identified during the planning process are reviewed regularly throughout the year. The Board receives monthly reports and management accounts and reviews the overall Group performance against budget and the latest forecasts for the current year. Similarly, each subsidiary and divisional management team meets regularly to monitor performance.

Internal Compliance and Control

The Board is responsible for and has undertaken a review of the Group's system of internal control and its effectiveness. This included an examination of the Group's self-certification procedures, risk management processes, internal audit reviews, external audit review of internal controls and regulatory compliance. As part of its review, the Board instructed an internal audit of corporate governance within the Group. The identification of key business risks, the evaluation of their financial and other implications and formulation of policies to manage such risks is the responsibility of the Directors. This system is designed to identify and manage, rather than eliminate risk and can provide only reasonable and not absolute assurance against material misstatement or loss.

Management reviews and self-certification reports from Directors and senior officers of each of the key subsidiaries or divisions are used to monitor compliance with the Group's internal financial, risk management and other controls.

The Group's internal audit function is responsible for providing assurance on the performance of the internal financial and risk management control system and computer operations and reports regularly to the Audit Committee. Internal audit work is focused on the areas of highest risk as agreed and prioritised by the Audit Committee. The scope of work, authority and resources of the internal audit function are reviewed by the Audit Committee at least annually.

Steps are being taken to embed internal control and risk management further into the operations of the business and to exploit areas of improvement which come to management and the Board's attention.

Sarbanes-Oxley Act

The United States Sarbanes-Oxley Act of 2002, introduces new and enhanced standards of corporate governance and business and financial disclosure which apply to British Energy as a non-US company with securities registered in the United States. Some of the new standards and rules affecting the Company are already in force. New standards directly applicable to the Company include certifications of the Annual Report on Form 20-F which is submitted to the Securities and Exchange Commission by the Chief Operating Officer and Chief Financial Officer (in the Company's case these are signed by the Chief Executive and the Interim Finance Director), changes to the role of the Audit Committee and new rules relating to internal controls. The Group is following these developments closely and intends to implement all necessary changes as the new rules come into force.

Corporate Social Responsibility

We plan to strengthen our whistle-blowing procedures during the year through the implementation of a procedure to allow staff to confidentially raise ethical concerns, suspicions of fraud or money laundering, suspicious accounting treatment or practices, and any other suspicious or non-compliant activity which an employee may observe. This procedure will involve direct referral to an external independent organisation which will record concerns and determine the appropriate person to investigate them and recommend any action required to address resulting issues.

The Company has published a separate Safety Health and Environment Report on its website. It is intended to replace this with a Corporate Social Responsibility Report, which will be published on-line later this year. This will include details of our record on safety and environmental performance. Further information on our approach to the environment and corporate social responsibility is contained on pages 23 and 24.

Going Concern

The Board considers it appropriate to prepare these accounts on a going concern basis for the reasons explained in note 1 to the financial statements for the year ended 31 March 2004.

Communication with Shareholders and Stakeholders

The Company recognises the importance of maintaining an ongoing relationship with its shareholders and stakeholders. It uses its Annual General Meeting as an opportunity to communicate with shareholders, and at that meeting a business presentation is made by the Chief Executive and by other Directors, if appropriate. It is the Company's policy that all Directors are available to answer shareholders' questions at the Annual General Meeting. In addition, the Chief Executive, the Chairman of the Audit Committee and the Interim Finance Director will meet with the Company's principal shareholders on request to discuss relevant issues when they arise. The Company seeks to ensure that the Directors, particularly the Non-Executive Directors, develop an understanding of the views of major shareholders through various routes including meetings and analysts' or brokers' briefings. The Company Secretary's office responds to numerous letters from shareholders on various issues throughout the year. Information sent to shareholders and copies of all Company announcements are made available on the Company's website – www.british-energy.com.

The notice of last year's Annual General Meeting held on 30 July 2003, was dispatched to shareholders not less than 20 working days before the meeting and details of proxy votes received were made available in accordance with the recommendations of the Combined Code.



Robert Armour

Company Secretary

17 June 2004