

# 2004 report by the Chairman

of EDF Board of Directors  
on corporate governance  
and internal control  
procedures

Financial security law  
of 1 August 2003  
(articles 117, 120 and 122)

When your world lights up



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# 1.

## INTRODUCTION

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In compliance with French law 2003-706 of 1 August 2003 on financial security, this report covers the preparation and organisation of Board of Director meetings as well as the internal control procedures implemented at EDF, including those that apply to consolidated subsidiaries.

The aim of this document is not an exhaustive presentation of all the control methods within the Group but rather to focus on the procedures concerning activities or risks deemed to be significant.

This report sets out the systems which were in place throughout 2004. Important changes implemented at the end of 2004 (transition to limited company status subsequent to the 17 November decree published in the French Official Journal of 19 November, new group organisational structure introduced on 15 December, etc.) will necessarily have consequences for internal control procedures and these will be analysed in the 2005 report.

The structure of this report is based on the Coso<sup>(1)</sup> reference system. The first section describes the internal control framework, including the functioning of the Board of Directors. The three following sections list the procedures designed to achieve the three recognised objectives of internal control:

- internal control procedures relating to the implementation and optimisation of operations;
- internal control procedures relating to the reliability of financial information;
- internal control procedures relating to compliance with laws and regulations.

The last section recalls the rapid development of internal controls within the EDF Group, as well as the process implemented to draw up and validate this report, in line with the financial markets authority (*Autorité des marchés financiers – AMF*<sup>(2)</sup>) recommendations.

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(1) Committee of Sponsoring Organizations of the Treadway Commission.

(2) See 2004 report from the AMF on corporate governance and internal control published 13 Jan 2005.

## 2.

# INTERNAL CONTROL FRAMEWORK

## 2.1.

### Preparation and organisation of Board of Director meetings

#### 2.1.1. FUNCTIONING OF THE BOARD OF DIRECTORS

The Board of Directors determines the direction of Group activities and monitors the implementation of its guidelines. It deliberates on all the Group's strategic aims as well as on matters expressly entrusted to it by law or which it has reserved for itself.

The Board of Directors comprises eighteen members<sup>(1)</sup>: six representatives of the French State, six individuals with relevant experience appointed by decree as well as six elected employee representatives. In addition, the following attend Board meetings without the right to vote: representatives from the State Economic and Financial Control Commission, the Government Commissioner and the Secretary of the Works Council.

The Directors' five-year term of office expired during 2004 and a new Board of Directors was formed on 14 September 2004. It is the result, on one hand, of elections for six employee representatives held on 6 May 2004 and, on the other, the 8 September 2004 decree published in the *Journal Officiel* of

9 September, making way for the nomination to the Board of Directors of six representatives of the French State and six individuals with relevant experience.

On the recommendation of this new Board of Directors, Pierre Gadonneix was named Chairman and Chief Executive Officer by the 15 September 2004 decree published in the *Journal Officiel* of 16 September.

Following the 17 November 2004 decree, published in the *Journal Officiel* of 19 November, ratifying the status of *Électricité de France SA* as a limited company and the 19 November decree, published on 20 November, ratifying the nomination of the Board of Directors of *Électricité de France*, Pierre Gadonneix was named Chairman of the Board of Directors of *EDF SA* by the 24 November 2004 decree, published in the *Journal Officiel* of 26 November.

Three Chief Operating Officers were nominated by the Board of Directors on 30 November 2004 following their proposal by the Chairman.

#### 2.1.2. INTERNAL REGULATION OF THE BOARD OF DIRECTORS

The functioning of the Board of Directors is supported by internal regulation voted by the directors:

- Until 14 December 2004, when new inter-

(1) See law relating to the democratisation of the public sector of 26 July 1983.

nal regulation was voted, the rules governing the functioning of the Board of Directors were exactly the same as in 2003. Thus to prepare its meetings and guarantee the quality of the debate, the Board of Directors was supported by a number of working groups, made up of directors.

- **The Investments Commission**, established in July 1947, is charged with examining all purchase contracts signed by the parent company amounting to €15 million or more. Chaired by the Chairman of the Board of Directors, it met five times in 2004.

- **The Operations Commission**, established in July 1947, analyses the Group's development as reflected in its operating budgets and prepares a report on the main lines of the Group's activities. Chaired by the Chairman of the Board of Directors, it met twice in 2004.

- **The Audit Committee**, established in October 1999, is chaired by a board member (a respected figure from outside the EDF Group) and comprises four members<sup>(1)</sup>. Prior to their submission to the Board, it comments on the half-yearly, annual and consolidated financial statements, the management report, the financial management review, the risk control policy and the internal audit programme; it also reviews the report of the Statutory Auditors. It met five times in 2004.

- **The Strategy Committee**, established in February 2000, is chaired by a board member (a respected figure from outside the EDF

Group) and comprises seven members. It gives its opinion on the Group's overall strategic aims, on the Group's business development policy, notably abroad, and on its industrial and sales policy. It met five times in 2004.

- **The Ethics Committee**, established in September 2001, is chaired by a board member (a respected figure from outside the EDF Group) and comprises six members. Its responsibility is to develop awareness of the ethical implications of Group strategic decisions. It reviews the annual Mediator and Ethics reports as well as changes in the functioning of the Board. It met six times in 2004.

The Board of Directors met eleven times in 2004. In addition to regular subjects of discussion, the Board addressed a number of specific issues in 2004 such as the Group's strategy on energy (EPR<sup>(2)</sup>), property and gas, the downstream end of the cycle and the Group's social and human resource policy.

- The transition to limited company status led to the drawing up of new internal regulation which was adopted on 14 December 2004. The main changes are as follows:

- The Operations and Investment Commissions have been abolished. The issues followed by the Operations Commission will become part of the agenda for the Board of Directors and a review is underway as to how to deal with the contracts, formerly the preserve of the Investment Commission.

*(1) Number increased to five as of 14 December 2004.*

*(2) European pressurized reactor.*

- The Audit Committee has one additional member and now consists of five directors.
- A Remuneration Committee was created, with three members, to be chaired by a board member (a respected figure from outside the Group). Its mission will be to comment to the Board of Directors, on compensation for the Chairman and CEO and for the Chief Operating Officers and for the conditions determining the remuneration of senior management (fixed and variable portions, method of calculation and indexation).
- The powers of the Chairman have been revised, and involvement of the Board of Directors will now be subject to the following levels:
  - acquisitions or disposals worth more than €200 million. This limit is reduced to €50 million for operations which are not in line with the Group's strategic objectives;
  - property deals exceeding €150 million;
  - contracts and endorsements involving sums of more than €100 million;
  - long-term contracts for the purchase or sale of energy, by the Group or by an exclusively controlled subsidiary, for quantities of over 7 TWh/year per operation.
- The Government Commissioner no longer attends Board of Director meetings.

The Board evaluates its method of functioning and the application of its internal regulation every year.

## 2.2.

### Ethics Policy

The ethics policy, as implemented at the Board of Directors meeting of 26 March 2003, aims to define a set of criteria for individual and collective professional conduct and to build the Group's reputation as an ethical organisation by implementing the Group's five core values: respect for the individual, respect for the environment, performance, solidarity and integrity. These five values are set out in an ethical charter, the circulation, promotion and adoption of which are the responsibility of management.

This ethics policy inspired, in 2004, the setting up or reworking of ethical codes in certain areas of the business such as procurement or use of IT systems. The ethical dimension is taken into account in fundamental processes such as recruitment, professional training and performance appraisal.

In addition, an ethical alert system has been set up, giving every employee and external partner the right to call the Group to account for any breach of its values. The Head of Ethics and the compliance team act for senior management in conducting a completely independent enquiry. They ensure that the decisions necessary to correct any proven breach are taken at the appropriate level. The Head of Ethics reports to the Group's executive management and to the Board's Ethics Committee.

## 2.3.

### Quality Assurance

Within two and a half years, EDF has made its Environmental Management System compliant with the ISO 14001 standard, one main requirement of which is strict compliance with environmental regulations. Thus, in April 2002, following audits carried out by an independent external body on Group entities whose activities are typical of EDF's lines of business, the company qualified for global quality certification for a period of three years. Note that in 2004 the Group was the subject of "follow up" audits in order to detect, sufficiently early, any shortfall likely to call into question the renewal of this certification on its expiry in April 2005.

## 2.4.

### Organisational structure and internal control bodies

#### 2.4.1. GROUP ORGANISATION AND MANAGEMENT PRINCIPLES

The organisation of the Group implemented at the beginning of 2002 was designed to streamline management and clarify lines of responsibility. It was based on the operating Branches, which were given a significant degree of autonomy, reporting to the Executive Committee (Comex) comprising the Chairman and the three Chief Operating Officers: Operations, Finance and Human Resources. This organisation remained unchanged throughout 2004.

On 15 December 2004, after consultation with employee representatives and presentation to the Board of Directors, the Chairman decided on changes to the Group's organisation. This new organisation had two major objectives: to improve the functioning of the Group as an integrated entity and to bring its operations closer to the decision-making process. To this end the Executive Committee has been extended to include nine new members, who are directly linked with operational and functional management.

The French transmission system operator (*Réseau de transport d'électricité – RTE*), in line with the law of 10 February 2000 giving it management independence, has developed its own control systems: an Audit Mission and Accounting and Financial Control.

In the same way, in conformity with the SPEEGEG<sup>(1)</sup> law of 9 August 2004, EDF's distribution network has created its own audit structure. A ruling from the Chairman on 10 September 2004 defined the principles of the functioning of this entity within the framework of the Group's own audit procedure (see § 2.4.3.2), which reconciles the confidentiality rules on sensitive information with the optimisation of resources allocated to the control function.

(1) *Public utility of electricity and gas and electricity and gas companies* (service public de l'électricité et du gaz et entreprises électriques et gazières).

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### 2.4.2. DELEGATION OF POWERS AND TECHNICAL AUTHORISATIONS

EDF's Board of Directors has granted its Chairman a delegation of authority and the Chairman has delegated part of his powers to certain of his immediate associates. Such delegation of power provides the basis for further delegation of powers to the main operating managers.

Thus, since June 2003, new delegations of power have allowed greater control to be exercised over procurement contracts, with only the Head of Procurement able to sign off on purchasing contracts.

The powers of the "nuclear energy operator" have been delegated to the Senior Executive Vice President in charge of Generation and Engineering who in turn delegates to the Senior Vice Presidents in charge of Nuclear Operations and Nuclear Engineering.

Each facility manager, subject to prior assessment of relevant skills, issues the technical authorisations that allow people to work in facilities (power stations, electricity transmission lines, etc.). These requirements apply to all workers, be they employees of EDF or of other outside providers.

The decree of 17 November 2004 ratifying the status of EDF SA provided that there would be no incidence on the delegation of powers in effect on that date. To take into account the change in the Group's organisation, these delegations will be reviewed in 2005.

### 2.4.3. INTERNAL CONTROL BODIES

#### 2.4.3.1. Financial Control

Financial Control, which reports to the Chief Financial Officer, performs the following tasks:

- It steers the processes of the Group's management cycle (medium term budgeting and planning arising from the Strategic Development Plan), summarises the major results of these processes and arbitrates between conflicting claims at Branch and Group levels by notifying the parties concerned, prior to decision-making, of the financial consequences of the planned projects and by providing analytical advice;

- It helps operational management to keep track of performance: monitoring of budget execution (involving forecast revision at least three times a year) is effected through regular broad-based performance reviews across all Branches (up to the end of 2004), Divisions and Subsidiaries;

- It acts as Group financial controller, notably by participating in investment monitoring and analysis to ensure economic and financial optimisation.

Financial Control is present at each managerial level. The financial controllers are members of the Management Committees of the entities to which they belong. Heads of Financial control in the Group's entities are directly or indirectly nominated and evaluated by the Group Chief Financial Officer.

#### 2.4.3.2. Group Audit Function

The Group's Audit charter was approved by the Executive Committee meeting of 10 March 2003. It defines the scope of internal



audit activity within the EDF Group, stipulating the auditors' duties, laying down a code of ethics and setting out the rights and obligations of the entities audited. This charter makes particular reference to the fact that the Audit Department defines the benchmark for the Group in matters of internal control. It was submitted to the Audit Committee just as the audit programme and its results are submitted to the same body for its opinion.

The control policy and organisation of EDF Group's Audit Function was decided by the Chairman on 21 October 2002. The policy will be adapted in 2005 to take into account the Group's new organisation.

The Group's Audit Function is made up of all the Group's control resources, at parent company and affiliate<sup>(1)</sup> level, and is responsible for "control of the control". The main principles are:

- audit is a management support function that operates independently of the audited entities and processes. It enhances consistency across the Group, notably because all the auditors use the same Group methodology based on international standards;
- the Chairman is responsible for supervising this function; he has delegated this task to the Head of Audit;
- members of the Executive Committee may ask the Audit Division for help in managing the risks associated with the business lines they supervise and in improving their results. The following tasks are entrusted to EDF's

Audit Division:

- formulate and update the Group's internal control policy;
- alert management to possible breakdowns in the control procedure;
- draw up the annual audit programme based on up-to-date mapping of Group risk. This programme is signed off by the Chairman after scrutiny by the Audit Committee;
- manage the network of auditors and coordinate internal control. To this end, in 2004, the Audit Division implemented a procedure designed to raise the professionalism of those involved and to set standards for internal control, particularly for the management and control of affiliates;
- coordinate the execution of all audit tasks across the Group.

Audits lead to recommendations which, after ratification by the entities audited, form the basis for action plans. During the year that follows an audit, the Audit Division monitors the progress of the implementation of these action plans.

Note that the Audit Division, following on from what was done in 2003, continued to draw up a self-diagnosis procedure relating to the internal control procedures of the main group entities.

#### 2.4.3.3. The Legal Division

In order to remain as close as possible to the decision-making bodies, at Group, Branch or regional level, the organisational structure of the Legal Division is based on that of the EDF Group. The Legal Division keeps track

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of legislative and regulatory changes. It is consulted whenever contracts have to be drawn up and whenever the legal risks of corporate projects have to be analysed. It also monitors major ongoing litigation. Its task leads it to issue warnings and to play a key role in avoiding litigation.

#### 2.4.3.4. Group Risk Management Division

The creation of the Group Risk Management Division in April 2003 marked the Group's commitment to adopting the most up-to-date standards of corporate governance, which recommend the implementation of a management structure integrating the issue of risk at Senior Executive Management level. Group Risk Management Division tasks are as follows:

- implement and manage the Group risk management process, while ensuring the monitoring of future regulatory obligations in this regard. All these activities are directed at identifying the main risks of any nature and the execution and updating of risk mapping at Group level. They also cover reporting and providing the Executive Committee, the Audit Committee and stakeholders with a clear vision of the risk map and the control systems to manage Group risk and likely developments in the risk profile. Lastly, the Division is responsible for consolidating and updating the Group's risk management policy;
- advise and alert the Chairman and the Executive Committee on the main risks at Group level and their likely development, as well as to flag early signs of potential future crises;

- ensure that the Group remains vigilant with regard to the risks to which its business activities expose society and the community;
- ensure, as of the beginning of 2004, the systematic control of exposure to energy market risk (wholesale electricity, gas, coal and oil markets) carried by the different Group entities operating in the wholesale markets (see paragraph 3.3.2);
- secure the investment control process (see paragraph 2.5).

The Group Risk Management Division has total independence in the execution of its tasks. It relies on the network of Group risk controllers, whose work it directs. The overall risk control process and the risk map are regularly presented to the Audit Committee.

## 2.5.

### Specific controls

#### 2.5.1. INVESTMENT APPROVAL PROCEDURE

The Group's investment committee (*Comité des Investissements Groupe – CIG*), presided by the Chairman, reviews and approves all planned investments worth more than €20 million. Since late March 2003, all CIG meetings are preceded by meetings of the Risk Committee, whose membership represents the Group's combined expertise at corporate level, thereby ensuring that the risks associated with investment projects submitted are subject to a comprehensive and in-depth analysis. A committee for commitments and shareholdings (*Comité des Engagements et*

*des Participations*) will take over and broaden, as of 2005, the responsibilities of the CIG.

### 2.5.2. MANAGEMENT AND CONTROL OF INFORMATION SYSTEMS (IS)

Overall Group strategy for information systems will be reviewed by a special IS strategy committee, chaired by the Chief Financial Officer and implemented as of the beginning of 2005.

The IS Group Committee (five meetings in 2004) is charged with the collective preparation of key decisions on information systems. It also consolidates the risks of this activity. It is chaired by the Senior Vice President, Head of Group Information Systems, who both directs the process and is accountable to the Executive Committee for the delivery of its objectives.

### 2.5.3. ADMINISTRATION AND SUPERVISION OF SUBSIDIARIES/AFFILIATES

Since 2002, executive management has benefited from the existence of a "Directorships of Subsidiaries/Affiliates" unit, whose job is to formulate and implement the processes required to carry out the Group's policy with regard to EDF's representation on the boards of subsidiaries/affiliates.

The Executives entrusted with the management of subsidiaries are required to define the "composition profile" of each Board of Directors. This profile should indicate the mix of collective and individual skills required of the Directors who will be representing EDF on the Boards of these subsidiaries/affiliates.

EDF appointees to Boards of subsidiaries are sent a letter setting out their remit and objectives.

### 2.5.4. EXTERNAL CONTROLS

Like all industrial and trading companies that go public, EDF is subject to the scrutiny of Statutory Auditors and financial market regulators. Thus the Statutory Auditors certify the EDF accounts at 31 December and, since 2003, also conduct a review on 30 June. Affiliate accounts are also reviewed by their own Statutory Auditors.

As a public sector corporation, EDF is also subject to special controls of its finances, management and internal control and purchasing by external public authorities: the French public accounting institution (*Cour des Comptes*), the State controllers, the Inspectorate of Public Finances, the Commission for Economic Affairs of the French National Assembly and Senate and the Markets Commission.

EDF is also regularly rated by financial, environmental and social responsibility rating agencies. Owing to the nature of its business activities, EDF is also subject to regulatory control by the French energy regulatory body (*Commission de régulation de l'énergie – CRE*) as well as being accountable, for its technology, to the government department responsible for nuclear safety (*direction générale de la Sécurité nucléaire et de la radioprotection*).

The results of all these different external review bodies feed into the Group's internal control process.

## 3.

# INTERNAL CONTROL PROCEDURES RELATING TO THE IMPLEMENTATION AND OPTIMISATION OF THE GROUP'S OPERATIONS

### 3.1.

#### Group risk mapping

In 2003, the Group Risk Management Division, with the support of the Audit Division, carried out a first comprehensive risk mapping exercise across all the Group's activities.

In January 2004, a summary of this first 2003 risk map was presented, respectively, to the Group's Management and Audit Committees as well as to the Statutory Auditors in February 2004.

The principle of a half-yearly update on this risk map consolidated at Group level and a half-yearly report to the stakeholders was adopted. The aim is to ensure that management has a good picture of any new risks as well as an up-to-date vision of the development of the risk portfolio and its control, consistent with the reporting schedule for the Group consolidated accounts.

### 3.2.

#### Risk management framework

The EDF Group has formulated a set of risk management policies:

- a currency, interest rate and cash flow risk management policy, approved by the Board of Directors in December 2001 and updated in December 2002;
- an energy market risk management policy, which has been deployed in most Group entities since 2001 (the Group Energy Market Risk Strategy has yet to be formally approved);
- a health and safety policy, signed by the Chairman in October 2003;
- a counterparty risk management policy, submitted to the Audit Committee in January 2004 and approved by the Board of Directors on 1 July 2004 (see Management Report - § 6.1);
- a Group insurance policy, approved by the Executive Committee in March 2003. This policy was presented to the Board of Directors on 1 July 2004 following a presentation on "storm risk cover policy" for the Distribution Network to the Group's Directors on 23 October 2004. The Board of Directors was updated on EDF Group's situation with regard to identified insurable risks and on the cover currently in place. It has also approved the

2004/2005 agenda and requested that the results of this work be reported to it in 2005. Any modification in the policy on insurance and insurable risk cover is henceforth consistent with the Group risk mapping process. This policy on insurance and insurable risk cover, as well as the other sector policies outlined above, are now an integral part of the Group's general risk control policy.

### 3.3.

#### **Risk management**

##### **3.3.1. FORMALISING ACTION PLANS AT ENTITY LEVEL**

At the time of the second risk-mapping exercise carried out in the 2004 first half, each entity embarked upon the formalisation of its action plan in order to guarantee a satisfactory level of control of risks identified.

##### **3.3.2. CONTROL OF ENERGY MARKET RISK**

As energy markets (electricity, gas, coal and oil) develop, energy company risk management procedures are increasingly scrutinised by the unions, rating agencies, creditors, the regulator and legislators. For this reason, the issue of controlling the impact of energy market risk is right at the centre of the development of the Group's different activities (generation, marketing, trading) and is a constant priority for Group management. Thus, in 2001, the Group created a Group Energy Market Risk control function to ensure:

- the formulation of the Group's policy on energy market risk;
- the systematic control of exposure and limits for the entities operating in the energy markets;
- the consolidation of the Group's exposure to energy market risk;
- the analysis of market risk associated with investment projects, disposals, development projects and long-term contracts.

In order to strengthen the control procedures, it was decided in March 2004 to embed this function in the Group Risk Management Division.

##### **3.3.3. CONTROL OF INVESTMENT RISK**

The 2003 implementation of a standard methodology for analysing development projects was aimed at strengthening the safeguards around all acquisitions, mergers and disposals. The purpose of this system is to take the full potential impact of a project into account and, particularly, to assess a number of stress scenarios. The screening of risks upstream from the Investment Committee is based on this framework. Adjustments will be made in 2005 based on the feedback received in September 2004.

At the same time, a reference framework methodology for analysing investment risk within the company's core business activities was implemented at the end of April 2004. Its principal aim is to factor analysis of the impact of the Group's major risks into the decision-making process.

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### 3.3.4. FINANCIAL RISK CONTROL

The Group's international development has led to the creation of a specific, independent entity charged with managing financial risk at Group level.

These include foreign exchange and interest rate risks as well as counterparty risk. This entity:

- defines Group financial risk management policy;

- oversees its implementation (secondary control);

- verifies that the methods, tools and indicators applied are consistent across the Group;

- consolidates risk exposure at Group level;

These processes are currently being deployed throughout the Group.

## 4.

### INTERNAL CONTROL PROCEDURES RELATING TO THE RELIABILITY OF FINANCIAL INFORMATION

#### 4.1.

##### **Accounting principles and standards**

The accounting standards used by the EDF Group comply with French regulations and, at the same time, systematically favour options that are compatible with international standards (IFRS). The main differences relate to:

- the accounting of retirement and other post-employment benefits in the French entities governed by the IEG regime, which will be taken into account in 2005 with the implementation of the new pension funding arrangement foreseen by the law of 9

August 2004. The accounting option set forth by the French law of not provisioning the pension liability was maintained as of 31 December 2004;

- the accounting of financial instruments, for which the adoption of IAS 32 and 39 will be taken into account in 2005.

As for the concessions, the IFRIC interpretation is expected in 2005 and the Group will adjust the accounting treatment consequently.

The management report will include a special version of the 2004 accounts under IFRS accounting rules (excluding IAS 32 and 39) showing the main impact on the balance

sheet and the income statement. As of 1 January 2005, the Group will move to IFRS accounting standards. The accounting rules and methods are outlined in the Group's accounting principles manual.

## 4.2.

### **Procedures for drawing up and controlling unbundled accounts**

In compliance with French law<sup>(1)</sup>, EDF produces unbundled accounts for each line of business: generation, transmission, electricity distribution and other activities. These accounts are prepared in compliance with principles of unbundled accounts and with the recommendations made by the energy regulatory body, CRE. After scrutiny by the Statutory Auditors, the accounts are submitted to the Audit Committee and then to the Board of Directors.

## 4.3.

### **Procedure for drawing up and controlling consolidated financial statements**

EDF has published consolidated financial statements every half year since 2003. The consolidated financial statements are sub-

mitted to the Audit Committee then to the Board of Directors.

The consolidated financial statements are based on data entered locally by each entity (parent company units and affiliates) in line with Group standards. Local data including a balance sheet, income statement and notes to the financial statement are drawn up in accordance with a common chart of accounts.

Amongst the established control procedures, those pertaining to assets, off-balance sheet commitments and cash management must be highlighted:

- group assets are valued on their acquisition date at their cost price. The gradual use of the assets is accounted for by depreciation. Estimated management data is checked to make sure that the carrying value of assets has not been overstated in relation to whichever of the two following values is the higher: value in use or market value, if available. The value in use is calculated using the future discounted cash flow method. Discount rates take into account the cost of capital and the specific risks of each business line;
- off-balance sheet financial commitments are also subject to investment authorisation procedures. They are revalued every time the accounts close. The annual accounts provide information on the amount of off-balance sheet commitments, in keeping with the Group's accounting standards. During 2004, a reminder of the rules relating to off-balance sheet commitments and an awareness campaign in all the Group businesses secured

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the reliability of the figures put forward for the 31 December 2004 accounts. An internal audit confirmed the quality of the work undertaken;

- a system for the delegation of power, control and reporting was established in 2004 for debt and cash management within the Corporate Finance and Cash Management Divisions.

#### 4.4.

#### **Internal control on the quality of the parent company's accounting**

The Accounting Division defines the reference system for controlling the degree of accounting quality that must be reached in the parent company. This system is based on major processes that cut across the Group's organisational structure: sales, purchases, personnel costs, fixed assets, inventories, cash flow, taxation and the drawing up of accounts. It specifies in particular what test criteria to use, the recommended random sampling methods and the reports required. The procedures for controlling the drawing up of accounts are mainly designed to verify that the accounts are accurate and complete. They also check that the principle of

separate accounting periods is respected, that book entries meet legal requirements, that the processes have been secured, that inventories have been carried out, that accounts are vouched for on a monthly basis, that the provisions booked in the accounts accurately reflect the depreciation of asset values and the company's obligations and that centralisation operations are reliable and complete.

The quality of the accounts produced by the Branches is ensured by contractual relationships with the Accounting Division. At each management level, an annual certificate is issued at the end of the accounting period, certifying that the accounting gives a true and fair view of the previous accounting period and highlighting improvements that need to be made in the next accounting period. Several audits are scheduled that focus on the scope of the accounting function.

At corporate level, formal checks are carried out notably on the strict equality of treatment of internal transfers between accounting entities and of entries relating to fixed assets and provisions.

Central controls on consistency and plausibility are also carried out, analysing account variations and their balances at the end of the period.



#### 4.5.

##### Action undertaken in 2004

In anticipation of the publication of the 2006 accounts in mid-February 2007, the Accounting Division strengthened in 2004 the quality control process for the drawing up of closing accounts to meet the requirements of the new accounting timetables (shorter lead-time for the drawing up of accounts, monthly closing and principle of separate accounting periods). The process of internal control of the drawing up of accounts was adapted and broadened to include the new sales and marketing organisations.

The process of integrating financial information systems was advanced, notably in the parent company, with the continuation of the SAP programme.

Measures to ensure better confidentiality of financial information across the company were pursued.

Measures were taken to strengthen the precision and completeness of information on off-balance sheet commitments.

#### 4.6.

##### 2005 action plan

Measures will be taken to guarantee the respect of obligations arising from the company's status as a limited company and the prospective share capital opening announced by the government, as well as to ensure the quality of published information arising as a result.

The emphasis will be on strengthening the quality of analysis and input associated with the drawing up of accounts produced locally.

To contribute to the level of quality sought, the Accounting Division will continue to improve the internal control process for accounting and finance by:

- increasing the level of dialogue with Group entities;
- adapting the control reference framework to sales processes and financial security;
- backing a more global approach to strengthening the Group's internal control procedures.

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## 5.

### CONTROL PROCEDURES RELATING TO COMPLIANCE WITH LAWS AND REGULATIONS

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In the industrial operations, there are many more control procedures than those outlined above (see paragraph 2.3 "Quality Assurance"):

In nuclear operations, two authorities are particularly worthy of note:

- **The Inspector General for Nuclear Safety (IGSN)** who, on behalf of the Chairman, makes sure that all aspects of safety and radioprotection concerns are fully taken into account and are the subject of a published annual report.
- **The Nuclear Inspection**, an entity direct-

ly attached to the Nuclear Operations Division, whose job is to check the level of safety in the different entities of the Nuclear Generation department (*Direction de Production Nucléaire*).

In the other areas (for example, the control of pressure devices and the inspection of dams), each entity is responsible for defining and implementing adequate control procedures.

Control procedures also exist for compliance with regulations on working conditions, labour law and social benefits.

## 6.

# THE DYNAMICS OF CHANGE

For several years, changes in the Group's organisation and modus operandi have allowed EDF to clarify and strengthen the effectiveness of internal control procedures with:

- the creation of several specialised committees to support the Board of Directors;
- the delegation of responsibility for results to Group entities;
- the creation and reinforcement of corporate divisions playing specific roles in the control process (the Legal Division, the Financial Control Division, the Risk Management Division, the Group Audit Function, etc.)

The implementation of an operational risk control procedure, the confirmation of the Group's ethical approach, the drive to standardise and speed up the drawing up of consolidated financial statements (notably in

view of the new accounting standards) and, more recently, the implementation of a new Group organisation are all part of this dynamic aimed at continuous improvement.

The Financial Security Law is an opportunity to build on this dynamic by involving the Group's operations management. This is particularly illustrated by the execution of auto-diagnoses on internal control procedures implemented in the different Group entities. This report, based on the 2003 version, was produced by a work group reporting to the Audit Division and includes contributions from the Legal, Group Risk Management and Accounting Divisions as well as the General Secretary of the Board of Directors and the Chairman's Office. Other contributions came from the Ethics, Compliance and Information Systems Divisions.

This report has been reviewed by, successively, the Chief Operating Officers and the Audit Committee (14 March 2005) and approved by the Board of Directors (16 March 2005). It was also discussed with the Statutory Auditors.



Paris, 16 March 2005,  
EDF Chairman  
Pierre Gadonneix

*This is a free translation into English of the independent auditors' report on the report prepared by the President of the Board of EDF, on the internal control procedures relating to the preparation and processing of accounting and financial information, signed and issued in the French language and is provided solely for the convenience of English speaking readers.*

*This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

## 7.

### INDEPENDENT AUDITOR'S REPORT

**INDEPENDENT AUDITORS' REPORT, PREPARED IN ACCORDANCE WITH ARTICLE L. 225-235 OF THE FRENCH CODE DE COMMERCE, ON THE REPORT PREPARED BY THE PRESIDENT OF THE BOARD OF EDF, ON THE INTERNAL CONTROL PROCEDURES RELATING TO THE PREPARATION AND PROCESSING OF ACCOUNTING AND FINANCIAL INFORMATION.**

Year ended 31 December 2004

In our capacity as independent auditors of EDF, and in accordance with article L.225-235 of the French Code de commerce, we hereby report to you on the report prepared by the President of your company in accordance with the requirements of article L.225-37 of the French Code de commerce for the year ended December 31, 2004.

It is for the President to give an account, in his report, notably of the conditions in which the duties of the board of directors are prepared and organized and the internal control procedures in place within the company.

It is our responsibility to report to you our observations on the information set out in the President's report on the internal control procedures relating to the preparation and processing of accounting and financial information.

We performed our procedures in accordance with the professional guidelines applicable in France. These guidelines require us to perform procedures to assess the fairness of the information set out in the President's report, on the internal control procedures relating to the preparation and processing of accounting and

financial information. These procedures notably consisted of obtaining an understanding of :

- the objectives and general organization of internal control, as well as the internal control procedures relating to the preparation and processing of accounting and financial information, as set out in the President's report;

- the company's procedures supporting the information given in the President's report.

On the basis of the procedures we have performed, we have no matters to report in connection with the information given on the company's internal control procedures relating to the preparation and processing of accounting and financial information, set out in the President's report, prepared in accordance with article L.225-37 of the French Code de commerce.

Neuilly-sur-Seine, Paris-La Défense and Paris, March 16, 2005

#### The Independent Auditors

##### **DELOITTE & ASSOCIÉS**

Amadou RAIMI    Tristan GUERLAIN

##### **ERNST & YOUNG Audit**

Patrick GOUNELLE    Claire NOURRY

##### **MAZARS & GUÉRARD**

Jean-Louis LEBRUN    Guy ISIMAT-MIRIN

**Internal control**

2004 Chairman's Report

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Corporate and Commercial Communication Division  
Audit Division