National Grid Gas plc
Annual Report and Accounts 2016/17

Company number 2006000

Contents

National Grid Gas plc Annual Report and Accounts 2016/17

Overview ... **1**
What we do - Gas ... 2
What we do – Regulation ... 3
Principal Operations - Overview ... 6
Our purpose, vision, strategy and values ... 10
Our strategic objectives ... 11
Progress against objectives - key performance indicators ... 12
Strategic Report ... **13**
Operating environment ... 13
Our business model ... 14
Our people ... 16
Internal control and risk management ... 18
Financial review ... 24
Corporate Governance ... 29
Business separation ... 37
Directors' Report ... 38
Introduction to the financial statements ... **39**
Statement of Directors' responsibilities ... 40
Independent Auditors' report ... 41
Basis of preparation ... 43
Recent accounting developments ... 45
Consolidated income statement ... 47
Consolidated statement of comprehensive income ... 48
Consolidated statement of changes in equity ... 49
Consolidated statement of financial position ... 50
Consolidated cash flow statement ... 51
Notes to the consolidated financial statements ... 52
Company accounting policies ... 87
Company balance sheet ... 91
Company statement of changes in equity ... 92
Notes to the Company financial statements ... 93
Glossary and definitions ... 101

Overview

About National Grid Gas plc

National Grid Gas plc (National Grid Gas) is a subsidiary of National Grid plc (National Grid), based in the UK, where we own and operate the regulated gas transmission network and provide gas metering services. We play a vital role in connecting millions of people safely, reliably and efficiently to the energy they use.

Up to 1 October 2016 we owned and operated four gas distribution networks comprising approximately 131,000 kilometres (81,400 miles) of pipeline, transporting gas from the National Transmission System (NTS) to around 10.9 million consumers on behalf of 41 gas shippers. On 1 October 2016 we sold the Gas Distribution business and associated assets to National Grid Gas Distribution Limited, a fellow National Grid group undertaking. As a result of the sale of the Gas Distribution business, we report the earnings of the Group separately from the Gas Distribution business which we report within 'discontinued operations'. While preparing the business for sale, we maintained our focus on operational delivery, which resulted in continued solid performance for Gas Distribution.

The overall management and governance of National Grid Gas is the responsibility of its Board of Directors. Strategic direction is determined by our ultimate parent company, National Grid. Our Directors are listed on page 38.

More information on the management structure of National Grid can be found in the National Grid plc Annual Report and Accounts 2016/17 and on National Grid's website at www.nationalgrid.com.

Financial highlights

	2016/17+ £m	2015/16+ £m	Percentage change
Operating profit	**464**	573	(19%)
Adjusted operating profit[1]	**573**	573	0%
Cash generated from operations	**723**	729	(1%)
Regulated assets[2]	**5,755**	5,594	3%

1. See page 24 for further details
2. See page 28 for further details.
+ Represents continuing operations only, comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

	2016/17+ £m	2015/16+ £m
Return on equity:		
Gas Transmission	**10.8%**	12.5%

Non-financial highlights

	2016/17+	2015/16+
Number of employees	**1,925**	2,114
Network reliability:		
Gas Transmission	**99.975%**	100%

+ Represents continuing operations only, comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

Our principal operations

We own and operate the gas national transmission system, with day-to-day responsibility for balancing supply and demand. Our network comprises approximately 7,660 kilometres (4,760 miles) of high-pressure pipe and 618 above-ground installations. Other activities include National Grid Metering. See page 9.

What we do - Gas

The gas industry connects producers, processors, storage and transmission and distribution network operators, as well as suppliers to industrial, commercial and domestic users.

The UK energy industry has four main sectors.

1. Production and importation

There are seven gas reception terminals, three LNG importation terminals and three interconnectors connecting Great Britain (GB) via undersea pipes with Ireland, Belgium and the Netherlands. Importers bring LNG from the Middle East, the Americas and other places.

We do not produce gas. Gas used is mainly sourced from gas fields in the North and Irish seas, piped from Europe and imported as liquefied natural gas (LNG).

2. Transmission

The transmission system includes pipes, compressor stations and storage facilities, including LNG storage. They connect production through terminals to the distribution systems.

Gas enters the transmission system through importation and reception terminals and interconnectors and may include gas previously held in storage. Compressor stations located along the network play a vital role in keeping large quantities of gas flowing through the system, particularly at times of high demand.

The gas transmission system has to be kept constantly in balance, which is achieved by buying, selling and using stored gas. This means that, under normal circumstances, demand can be met. We are the sole owner and operator of gas transmission infrastructure in Great Britain.

3. Distribution

Gas leaves the transmission system and enters the distribution networks at high pressure. It is then transported through a number of reducing pressure tiers until it is finally delivered to consumers.

For six months National Grid Gas owned four of the eight regional distribution networks. The Gas Distribution business and associated assets were sold on 1 October 2016 to National Grid Gas Distribution Limited, a fellow National Grid group undertaking.

4. Supply

Pipeline shippers bring gas from producers to suppliers, who in turn sell it to customers.

We do not supply gas, however we own National Grid Metering, which provides meters and metering services to supply companies, under contract.

Customers pay the supplier for the cost of gas and for its transportation. We transport the gas through our network on behalf of shippers, who pay us transportation charges.

What we do – Regulation

Our business operates as a regulated monopoly. We have one economic regulator for our business, Ofgem. The regulator safeguards customers' interests by setting the level of revenues we are allowed to recover, ensuring we provide value for money while maintaining safe and reliable networks, and deliver good customer service.

How we make money from our regulated assets

Our licence, established under the Gas Act 1986, as amended (the Act) requires us to develop, maintain and operate economic and efficient networks and to facilitate competition in the supply of gas in Great Britain (GB). It also gives us statutory powers. These include the right to bury our pipes under public highways and the ability to use compulsory powers to purchase land so we can conduct our business.

Our network is regulated by Ofgem, which has established price control mechanisms that set the amount of revenue our regulated businesses can earn. Price control regulation is designed to make sure our interests, as a monopoly, are balanced with those of our customers. Ofgem allows us to charge reasonable, but not excessive, prices. This gives us a future level of revenue that is sufficient to meet our statutory duties and licence obligations, and make a reasonable return on our investment.

The price control includes a number of mechanisms designed to help achieve its objectives. These include financial incentives that encourage us to:

- efficiently deliver by investment and maintenance the network outputs that customers and stakeholders require, including reliable supplies, new connections and infrastructure capacity;
- innovate in order to continuously improve the services we give our customers, stakeholders and communities; and
- efficiently balance the transmission networks to support the wholesale markets.

The Gas Distribution business and associated assets was sold on 1 October 2016 to National Grid Gas Distribution Limited, a fellow National Grid group undertaking. National Grid plc announced on 31 March 2017 that a majority interest in the UK Gas Distribution business was sold to a consortium of investors. National Grid has retained a 39% equity interest in the new separate Gas Distribution business.

The UK Gas Transmission (UK GT) and UK Gas Distribution (UK GD) businesses operate under six separate price controls in the UK. These comprise two for our UK GT operations, one as transmission owner (TO) and one as system operator (SO); and one for each of the four regional gas distribution networks. While each of the six price controls may have differing terms, they are based on a consistent regulatory framework.

There is no impact on the price control following the sale of the Gas Distribution business. The six price controls, as mentioned above, remain in force. National Grid Gas will carry operating within two of the price controls, and the UK Gas Distribution business has responsibility for operating within the price controls relating to its four gas distribution networks.

In addition to the six price controls, there is also a tariff cap price control applied to certain elements of domestic metering and daily meter reading activities carried out by National Grid Metering.

RIIO Price Controls

Our regulatory framework is called RIIO (revenue = incentives + innovation + outputs) and lasts for eight years until March 2021. The building blocks of the RIIO price control are broadly similar to the historical price controls used in the UK. However, there are some significant differences in the mechanics of the calculations.

How is revenue calculated?

Outputs

Under RIIO the outputs we deliver are clearly articulated and are integrally linked to the calculation of our allowed revenue. These outputs have been determined through an extensive consultation process, which has given stakeholders a greater opportunity to influence the decisions.

The six output categories are:

Safety - ensuring the provision of a safe energy network.

Reliability (and availability) - promoting networks capable of delivering long-term reliability, as well as minimising the number and duration of interruptions experienced over the price control period, and ensuring adaptation to climate change.

Environmental impact - encouraging companies to play their role in achieving broader environmental objectives, specifically, facilitating the reduction of carbon emissions, as well as minimising their own carbon footprint.

Customer and stakeholder satisfaction - maintaining high levels of customer satisfaction and stakeholder engagement, and improving service levels.

Customer connections - encouraging networks to connect customers quickly and efficiently.

Social obligations (GD only) - extending the gas network to communities that are fuel poor where it is efficient to do so, and introducing measures to address carbon monoxide poisoning.

Within each of these output categories are a number of primary and secondary deliverables, reflecting what our stakeholders want us to deliver over the remaining price control period. The nature and number of these deliverables varies according to the output category, with some being linked directly to our allowed revenue, some linked to legislation, and others having only a reputational impact.

Totex

Ofgem, using information we have submitted, along with independent assessments, determines the efficient level of expected costs necessary to deliver our outputs. Under RIIO this is known as totex, which is a component of total allowable expenditure, and is the sum of what was defined in previous price controls as operating expenditure (opex), capital expenditure (capex) and, in GD price controls, mains replacement expenditure (repex).

A number of assumptions are necessary in setting the outputs, such as certain prices or the volumes of work that will be needed. Consequently, there are a number of uncertainty mechanisms within the RIIO framework that can result in adjustments to totex allowances if actual prices or volumes differ from the assumptions. These mechanisms protect us and our customers from windfall gains and losses.

Where we under- or over-spend the allowed totex for reasons that are not covered by uncertainty mechanisms, there is a sharing factor. This means the under- or over-spend is shared between us and customers through an adjustment to allowed revenues in future years. This sharing factor provides an incentive for us to provide the outputs efficiently, as we are able to keep a portion of savings we make, with the remainder benefiting our customers.

This sharing factor is one of the ways that RIIO has given innovation more prominence. Innovation includes traditional areas such as new technologies, as well as the broader challenge of finding new ways of working to deliver outputs more efficiently. This broader challenge has an impact on everyone in our business.

Allowances to fund totex costs are split between fast and slow money – a concept under RIIO, based on a specified percentage that is set for the duration of the price control. Fast money represents the amount of totex we are able to recover in the year. Slow money is added to our regulated asset value (RAV) – effectively the regulatory IOU. For more details on the fast/ slow money rates and sharing factors under RIIO, please see the table on page 5.

In addition to fast money, in each year we are allowed to recover a portion of the RAV (regulatory depreciation) and a return on the outstanding RAV balance.

Return on equity and cost of debt – regulated assets are funded through a mixture of debt and equity. The equity portion earns a ‘return on equity’. This represents the profit we can earn on our investment in regulated assets. The debt portion earns an allowance based on the cost of debt (interest costs). Ofgem use an external benchmark interest rate to incentivise us to raise debt efficiently. The benchmark interest method also provides an opportunity to outperform our regulatory allowance. The allowed rates of return on equity and debt are included in the table on page 5.

Depreciation of regulated assets – the value of regulated assets is depreciated over an anticipated lifespan. The amount of depreciation is included in our allowed revenue, which represents the repayment of the amount we have invested in the asset.

The asset life for regulatory depreciation is 45 years for Gas Distribution and GT TO RAV additions. For the GT SO the asset life is 7 years.

We are also allowed to collect additional revenues related to non-controllable costs.

Performance against incentives – our price controls include incentives that are designed to encourage specific actions, such as reducing greenhouse gas emissions.

The incentive mechanisms can increase or decrease our allowed revenue and result from our performance against various measures related to our outputs. RIIO has incentive mechanisms that encourage us to align our objectives with those of our customers and other stakeholders. For example, performance against our customer satisfaction targets can have a positive or negative effect of up to 1% of allowed annual revenues. Most of our incentives affect our revenues two years after the year of performance.

Timing – our regulated revenue entitlements are set based on our regulatory price controls. We use forecast energy volumes that we expect to deliver to set the billing tariff. Where there is a difference between the actual and estimated energy volumes, the amount of revenue we collect will be different. We recover or repay this difference in a future year.

Mid period review

Under the RIIO controls, we are required to deliver agreed outputs for consumers and are funded to cover the costs of delivering these. The eight year price control includes a number of uncertainty mechanisms to take account of the fact that some outputs and funding cannot be set with certainty at the start of the period. One of these uncertainty mechanisms is the review of outputs.

During the eight year period of the price control our regulator included a provision for a potential mid-period review, with scope driven by:

- changes to outputs that can be justified by clear changes in government policy; and
- the introduction of new outputs that are needed to meet the needs of consumers and other network users.

In May 2016, Ofgem announced a mid-period review of the RIIO-T1 price control looking at specific output measures in Gas Transmission. The outcome of the review was that Ofgem removed outputs relating to a pipeline project at Avonmouth and reduced allowances by £169 million in Gas Transmission. These changes flow through to an adjustment to our revenues from April 2018.

Allowed returns

The cost of capital allowed under RIIO is as follows:

	Transmission	Distribution+
Cost of equity (post-tax real)	6.8%	6.7%
Cost of debt (pre-tax real)	iBoxx 10 year simple trailing average index (2.38% for 2016/17)	
Notional gearing	62.5%	65.0%
Vanilla WACC*	4.03%	3.89%

**Vanilla WACC=cost of debt x gearing + cost of equity x (1-gearing)*

+ This was a National Grid Gas business until 1 October 2016.

Sharing factors and fast money

The sharing factor means that any over- and under-spend is shared between the businesses and consumers. The shared figures displayed in the table below are the sharing factors that apply to Gas Transmission and Distribution.

Sharing factors under RIIO are as follows:

Gas Distribution[4]	North West	East of England	West Midlands	London
	Replacement expenditure: Stepped decline from 50% in 2013/14 to 0% in 2020/21 in seven equal instalments of 7.14% per annum			
Fast[1]	73.90%	73.37%	75.05%	76.53%
	Replacement expenditure: Stepped increase from 50% in 2013/14 to 100% in 2020/21 in seven equal instalments of 7.14% per annum			
Slow[2]	26.10%	26.63%	24.95%	23.47%
Sharing[5]	63.04%			

Gas Transmission	Transmission Operator	System Operator
Fast[1]	Baseline[3] 35.6%, Uncertainty 10%	62.60%
Slow[2]	Baseline[3] 64.4%, Uncertainty 90%	37.40%
Sharing[5]	44.36%	

1 Fast money allows network companies to recover a percentage of total expenditure within a one year period.
2 Slow money is where costs are added to RAV and, therefore, revenues are recovered slowly (e.g. over 45 years) from both current and future consumers.
3 The Baseline is the expenditure that is funded through ex ante allowances, whereas the uncertainty adjusts the allowed expenditure where the level outputs delivered differ from the baseline level, or if triggered by an event.
4 This was a National Grid Gas business until 1 October 2016.
5 The sharing factor is the proportion of over and under spend retained by National Grid Gas.

For more information on RIIO, including incentive mechanisms, please see the relevant investor fact sheets on the Investor Relations section of our website, www.nationalgrid.com.

Principal Operations - Overview

Our regulated businesses delivered a solid financial performance in the fourth year of RIIO. We aim to create value for our stakeholders by focusing on performance and making sure our processes are as efficient as they can be.

In line with our plans, we separated Gas Distribution into a stand-alone business. While preparing the business for sale and a new ownership structure, we maintained our focus on operational delivery, which resulted in continued solid performance for Gas Distribution.

We welcomed the conclusion of the mid-period review of the RIIO price control for Transmission which has given us certainty over our core revenues for the remaining RIIO period. Ofgem made some adjustments to allowances in Gas Transmission for outputs no longer needed in the RIIO period.

Earlier in 2017, The Department for Business, Energy and Industrial Strategy (BEIS) confirmed, through the ‘Building our Industrial Strategy’ green paper, its intention to focus on developing technical education and skills. National Grid plc received an ‘Outstanding’ grade from Ofsted, for the third time consecutively, on the standard of apprentice training offered by our Academy. Addressing the skills shortage, and providing high-quality training, remains important to us.

Set against these developments, our businesses have continued to perform well during the last year with continued world class safety levels and network reliability.

Principal Operations - Gas Transmission

What we do

We own and operate the gas national transmission system, with day-to-day responsibility for balancing supply and demand. Our network comprises approximately 7,660 kilometres (4,760 miles) of high-pressure pipe and 618 above-ground installations.

Market Context

The UK's gas market and sources of gas are changing. Domestic demand has fallen over the last five years and a significant increase is not expected in future years. The UK continental shelf (UKCS) now makes up less than half our total gas supply, with the remainder coming from Norway, continental Europe, or further afield via shipped imports of LNG.

Overall, supply capacity now exceeds peak demand by more than 30%, giving our customers significant flexibility over which sources of gas they choose to meet demand. Flexible sources of supply, such as LNG importation terminals, interconnectors and storage sites, can respond to demand more quickly than traditional UKCS supplies. Therefore, our network needs to be able to respond to changing day-to-day and within-day supply and demand patterns.

We also need to prepare for an uncertain energy landscape in the long term. UK reliance on imported gas supplies will vary depending on the level of gas supply from the UKCS and the development of indigenous gas sources.

We are working closely with our customers and stakeholders to meet these operational challenges. We are focused on continuing to develop our network and services to meet their needs safely, reliably and efficiently.

Operational Performance

Our network reliability figures decreased slightly for Gas Transmission and are marginally below target this year. However, we continue to work on initiatives that aim to strengthen reliability, such as our asset health improvement work. This year, for example, we have made good progress on the Feeder 9 gas pipeline replacement project. This involves boring a five kilometre tunnel beneath the River Humber to replace a section of gas pipeline. We are also developing new technologies to deliver work faster and increase network reliability.

We have worked hard to find ways of operating more efficiently, so we can make our business more agile and competitive. For example, we initiated a project to upgrade some air compressor units, reducing carbon dioxide emissions by 1,228 tonnes, and yielding long-term financial savings of £2.42 million.

We installed new gas control systems – these will help us meet the challenges of the changing energy world and, therefore, help us balance gas even more efficiently, keeping costs to consumers down.

We have used our regulatory innovation funding to develop ways to serve our customers more effectively, provide greater value, and shape the energy systems of the future. Through Project CLoCC (Customer Low Cost Connections), for example, we're challenging every aspect of the current gas transmission customer connections process. It aims to reduce the time to connect from three years to less than one, and reduce the cost from up to £2 million to significantly less than £1 million. It will also make it easier for non-traditional customers to connect to the National Transmission System (NTS).

Shaping the future of energy

This year we launched a nationwide conversation on the Future of Gas to gather insights on the future role of gas and the gas transmission network. Gas will continue to be an important part of the mix in ensuring a secure energy supply at best value for consumers while Britain transitions to a low-carbon future. By engaging with stakeholders to understand what customers and end consumers value, this project will help us to identify optimal levels of future investment in the system and innovative ways to adapt our commercial arrangements.

At a European level, we have worked closely with organisations such as ENTSOG (the European Network of Transmission System Operators for gas) to implement a number of framework changes in a way that works for Britain's energy market and our customers.

Looking ahead

Our main focus is to drive a step change in core business performance. We have detailed plans in place to improve safety, our delivery for customers and our efficiency. We are continuing work in a number of priority areas.

Safety: build on, and further improve our safety culture and statistics through a review of our risk management approach.

Reliability: increase the amount of maintenance and replacement work on our assets, in line with our RIIO commitments and develop an improved asset health risk methodology.

Efficiency: improve the quality of data on our assets to further strengthen our investment decisions and to drive efficiencies in our project work. In response to customer feedback, work to reduce the time taken to connect customers to our network.

Innovation: continue to create value for customers and the wider industry through innovation development and implementation.

Emissions compliance projects: meet the European IED requirements by delivering our agreed asset enhancement and replacement programme.

System Operator

As Great Britain's System Operator (SO) we make sure supply and demand are balanced in real-time and we facilitate the connection of assets to the transmission system.

Market context

Sources of energy are changing. The changing location of gas being input into the transmission system will drive greater need for flexibility as the traditional north-south flow diminishes.

This makes our role in matching supply and demand more challenging, so we work with the market to make sure we have appropriate tools in place to balance the transmission system. We work with our customers and stakeholders to shape the future of the energy market, providing analysis and insight into the changing nature of energy. We also facilitate changes to the market frameworks to accommodate new technologies and ways of working, while considering how the role of the SO should evolve over time.

The SO is at the forefront of this debate helping to find solutions with industry.

Operational Performance

We continue to play a leading role in helping develop the UK's future energy strategy, and that of Europe. Our approach includes working with customers and stakeholders on initiatives such as the translation of new EU code requirements for gas, the development of new demand side services supporting the harmonisation of gas trading arrangements across Europe, our Future Energy Scenarios reports, and System Operability Framework workshops and webinars.

We are working hard across our business to place customers at the heart of our operations. We're holding workshops for customers so we can gain a more in-depth understanding of their requirements. We have also started to examine each point of contact they have with our Company, so we can identify where we can improve our processes and our customers' experience with us. We will be testing proposed improvements with customers before we implement them.

Priorities for the year ahead

We will continue to find better ways to provide timely, cost effective and innovative solutions to balance supply and demand for gas.

Market developments

We will continue to work with Ofgem and BEIS as they develop proposals to help meet the energy challenges of the future.

Customers and stakeholders

We will continue to develop our longer-term strategy to understand the issues that will affect our customers and stakeholders in the future, and plan how we will best support them.

Delivering energy

We will continue to support the evolution of market frameworks in the UK and Europe to enable new types of generation and demand to come forward in response as the energy landscape changes.

Principal Operations - Other activities

Other activities include National Grid Metering and other corporate activities.

National Grid Metering
National Grid Metering (NGM) provides installation and maintenance services to energy suppliers in the regulated market in Great Britain. It maintains an asset base of around 12.3 million domestic, industrial and commercial meters.

Customer satisfaction scores for NGM remain positive for domestic, industrial and commercial businesses. We continue to work with our customers on areas for improvement by exploring additional products and services so we can respond to the rapidly changing non-domestic sector.

Discontinued Operations

Gas Distribution
For the six months to 1 October 2016 we owned and operated four gas distribution networks comprising approximately 131,000 kilometres (81,400 miles) of pipeline, transporting gas from the NTS to around 10.9 million consumers on behalf of 41 gas shippers. The Gas Distribution business and associated assets was sold on 1 October 2016 to National Grid Gas Distribution Limited, a fellow National Grid group undertaking.

Operational performance
Our network reliability figures decreased slightly for Gas Distribution business however, while preparing the business for sale and a new ownership structure, we maintained our focus on operational delivery which resulted in a solid performance for the gas distribution business up to 1 October 2016.

Xoserve
On 1 October 2016, National Grid Gas's ownership of Xoserve reduced from 56.57% to 11% and therefore the results of the business cease to be consolidated after six months. Xoserve delivered transactional services on behalf of all the major gas network transaction companies in Great Britain, including National Grid. The results of Xoserve are included within discontinued operations.

Our purpose, vision, strategy and values

To make sure we are well positioned to respond to changes in the operating environment, we have evolved our purpose, vision, strategy and values.

Our purpose

Having a clear sense of what we stand for as a company and what it is that binds us all together is vitally important. This is what we call our purpose. In simple terms it's what drives our desire to serve our customers and it's that thing that makes us proud about the work we do.

Our purpose is to bring energy to life
In its simplest form 'bring energy to life' means getting the heat, light and power that customers rely on to their homes and businesses. But 'life' also means supporting the communities that we are a part of and live amongst to support the economic growth and sustainability of wider society.

Our vision

Our vision describes how we create value – not just today, but in the future too.

Our vision is: "We will exceed the expectations of our customers, shareholders and communities today and make possible the energy systems of tomorrow."

The needs of our customers, shareholders and communities are at the heart of everything we do. So, our vision statement clearly describes the ambitious challenge we have set ourselves – to make sure we deliver value for them every day.

Our vision also looks to the future, reminding us of the critical role we will play for future generations. We are already seeing changes in our energy system as more renewable and decentralised generation is introduced. To be relevant in this future, we have to play an active role in helping shape the energy landscape, and benefiting from what it provides.

Our strategy

We have three strategic priorities for our business that will help us achieve our vision.

1) Find new ways of optimising our operational performance
Our customers want and need us to be more efficient, so we must find ways to improve how we run our business. We have looked at enhancing our productivity and customer experience through more efficient and customer-focused processes. Given the scale of our core business, even small improvements will have a huge impact on our overall performance. Finding new ways of optimising our operational performance will be an important factor in our ability to compete and grow. It creates the financial capacity and the capability for us to future-proof our business.

2) Look for opportunities to grow our core business
Delivering solid operational performance provides us with a foundation to pursue other opportunities. We will continue to pursue business development opportunities that are close to our core business.

3) Make sure National Grid is better equipped for the future
We need to future-proof our business against the effects of a changing energy landscape. The operation of our networks is already affected by changes to the generation mix, while the needs and expectations of our customers are evolving.

Our values

We know that how we deliver is as important as what we deliver. If our purpose is the 'why', our values are the 'how'. They help shape our spirit, attitude and what guides us. We have to adapt and develop our values to align with the expectations of our customers and communities, without losing sight of the things that make us strong today.

Our values build on and protect our strong foundations while looking to the future. They're aligned to our purpose and help our people understand how we expect to achieve our purpose and vision for our customers and each other.

Every day we do the right thing and find a better way.

'Do the right thing' pulls together our foundational values – keeping each other and the public safe; complying with all the relevant rules, regulations and policies; respecting our colleagues, customers and communities; and saying what we think and challenging constructively. 'Find a better way' challenges us to focus on performance and continuous improvement for our customers, our shareholders and communities.

Our strategic objectives

We first set out our current strategy in our 2012/13 Annual Report and have continued to report on our progress against it since then. As we describe on pages 6 to 9, there is an extraordinary amount of change facing our industry, so we have evolved our purpose, vision, strategy and values (see page 10).

We aim to be a recognised leader in the development and operation of safe, reliable and sustainable energy infrastructure, to meet the needs of our customers and communities and to generate value for our investors. We measure our progress in creating value for our investors.

Strategic objective	Description	How we deliver	Relevant KPIs
Deliver operational excellence	Achieve world-class levels of safety, reliability, security and customer service.	Our customers, communities and other stakeholders demand safe, secure and reliable supply of their energy. This is reflected in our regulatory contracts where we are measured and rewarded on the basis of meeting our commitments to customers and other stakeholders.	Employee lost time injury frequency rate Customer satisfaction Network reliability Return on equity (ROE)
Engage our people	Create an inclusive, high-performance culture by developing all our employees.	It is through the hard work of our employees that we will achieve our vision, respond to the needs of our stakeholders and create a competitive advantage. Encouraging engaged and talented teams that are in step with our strategic objectives is vital to our success.	Employee engagement index Workforce diversity
Stimulate innovation	Promote new ideas to work more efficiently and effectively.	Our commitment to innovation allows us to run our networks more efficiently and effectively and achieve our regulatory incentives. Across our business, we explore new ways of thinking and working to benefit every aspect of what we do.	See principal operations section
Engage externally	Work with external stakeholders to shape UK and EU energy policy.	Policy decisions by regulators, governments and others directly affect our business. We engage widely in the energy policy debate, so our position and perspective can influence future policy direction. We also engage with our regulators to help them provide the right mechanisms so we can deliver infrastructure that meets the changing needs of our customers and stakeholders.	Community engagement and investment in education
Embed sustainability	Integrate sustainability into our decision-making to create value, help preserve natural resources and respect the interests of our communities.	Our long-term sustainability strategy sets our ambition to deliver these aims and to embed a culture of sustainability within our organisation.	Climate change Greenhouse gas emissions
Drive growth	Grow our core businesses and develop future new business options.	We continue to maximise value from our existing portfolio, while exploring and evaluating opportunities for growth. Making sure our portfolio of businesses maintains the appropriate mix of growth and cash generation is necessary to meet the expectations of our shareholders.	Regulated asset base growth

Progress against objectives - key performance indicators

The Board uses a range of financial and non-financial metrics, reported periodically, against which we measure performance.

Strategic element	Regulatory Output[1]	Key performance indicators (KPIs) and definition	Our performance	
Deliver operational excellence	**Safety**	**Employee lost time injury frequency rate (IFR)** Injuries resulting in employees taking time off work per 100,000 hours worked on a 12 month basis. Our ambition is to achieve a world-class safety performance of below 0.1.	**2016/17: 0.11[3] (Target: 0.1)** 2015/16: 0.13[3] (Target: 0.1)	
	Customer satisfaction	**Customer satisfaction** Our score in customer satisfaction surveys. Ofgem set a baseline target.	**Transmission:** **2016/17: 8.0 out of 10 (Target: 6.9[5])** 2015/16: 7.6 out of 10 (Target: 6.9[5])	**Distribution:** **2016/17: – (Target: 8.3[5])** 2015/16: 8.4 (Target: 8.3[5])
	Reliability	**Network reliability** Reliability of gas network as a percentage against the target set by Ofgem.	**Transmission:** **2016/17: 99.975%** **(Target: 100%)** 2015/16: 100% (Target: 100%)	**Distribution**: **2016/17: 99.998%** **(Target: 99.999%)** 2015/16: 99.999% (Target: 99.999%)
Engage our people	**Employee engagement**	**Employee engagement index[2]** Employee engagement index calculated using responses to National Grid's annual employee survey. Target is to increase the level of engagement compared with previous year.	**2016/17: 77%** 2015/16: 73%	
	Workforce diversity	**Workforce diversity** We measure the percentage of women and ethnic minorities in our workforce. While we have no specific target we aim to develop and operate a business that has an inclusive and diverse culture.	**Workforce diversity %** **2016/17: Women 33.7%** **Ethic minority: 9.3%** 2015/16: Women[3] 24% Ethnic minority[3] 7.1%	
Engage externally	**Community engagement and investment in education**	**Community engagement and investment in education[4]** Working with our communities is important in creating shared value for us as a business and the people we serve.	**2016/17: £5.8 million** 2015/16: £4.2 million	
Embed sustainability	**Environmental impact**	**Greenhouse gas emissions** Percentage reduction in greenhouse gas emissions. National Grid Target 2016/17 and 2015/16: 45% reduction by 2020 and 80% reduction by 2050.	Tonnes carbon dioxide **Transmission** **2016/17: 670,429** 2015/16: 408,492	
Drive growth		**Regulated asset growth** Maintaining efficient growth in the total Regulated Asset Value (RAV) base.	**2016/17: 3%** 2015/16: 1%	

[1] See pages 3 to 5 for explanation of regulatory outputs.
[2] Index represents performance for National Grid plc.
[3] Includes National Grid Distribution.
[4] Index represents performance for National Grid UK.
[5] Figures represent our baseline targets set by Ofgem for reward or penalty under RIIO.

Greenhouse gas emissions

National Grid has remained focused on greenhouse gas emissions reduction programmes to achieve the corporate commitment targets of 45% and 80% reduction in Scope 1 and 2 emissions by 2020 and 2050 respectively from the 1990 baseline. National Grid continues to look for innovations and efficiencies that will help us achieve targets. National Grid measure and report in accordance with the World Resources Institute and World Business Council on Sustainable Development Greenhouse Gas Protocol: Corporate Accounting and Reporting Standard (Revised Edition) for all six Kyoto gases, using the operational approach for emissions accounting. 100% of National Grid plcs Scope 1 and 2 emissions and 92% of Scope 3 emissions are independently assured against ISO 14064- 3 Greenhouse Gas assurance protocol. A copy of this statement of assurance is available on the National Grid website. See the National Grid plc Annual Report and Accounts for further information.

Strategic Report

Operating environment

Our operating environment is shaped by the regulatory choices governments make to respond to the changing needs of energy consumers. In meeting these demands, regulators seek to balance often conflicting objectives. In the last year we have seen a shift in focus to affordability and moving to a low carbon economy.

	Affordability	Security of supply	Sustainability
Commentary	The cost of the energy is an issue for consumers, industry, energy providers, regulators and governments. Consumers expect a reliable energy system that delivers gas when and where it is needed. They pay for the cost of this infrastructure and improvements to it through the network costs part of their energy bills. The costs are subject to regulatory approval.	The energy system is in a phase of transition from high to low carbon. Coal plants are closing down and being replaced with nuclear, renewables and gas, as well as emerging battery storage. During the transition, margins need to be monitored and actively managed as we move to a generation mix with greater volumes of intermittent generation.	Our world is changing as a result of human activity and its impact on the environment. The Paris Agreement sends a clear signal that the shift to a low-carbon economy is inevitable, and it is now accepted that sustainable business is good business – delivering value for people, the environment and business. This includes reducing greenhouse gas emissions, managing non-renewable resources, and preserving and protecting habitats and ecosystems.
Developments	The Government set out proposals for an industrial strategy that confirms the high priority placed on affordability of energy. Ofgem proposed a number of adjustments to allowances for Gas Transmission following its mid-period review of the RIIO-T1 price control. As new technologies are adopted, there are fears that low-income customers may not have access to cheaper, cleaner sources of energy.	Energy security remains a priority for the Government, and a number of balancing tools are available to manage capacity. The Department for Business, Energy and Industrial Strategy (BEIS) introduced amendments to the UK capacity market to improve long-term planning of capacity and reduce costs to consumers.	In December 2015, the Paris Agreement entered into force. The Agreement requires signatories to commit to reducing global greenhouse gas emissions with the aim of limiting increases in global average temperature. Investing in the low-carbon economy is a priority for the Government. The BEIS green paper on industrial strategy included a focus on developing education and skills for energy innovation.
Our response	Our regulated business continues to strive for greater efficiency to help offset the impact of costs for energy and capital investment programmes. We continue to find innovative ways to reduce both the time and cost to repair or replace assets, minimising the costs to consumers. We voluntarily set aside £150 million of the proceeds from the sale of a majority interest in our Gas Distribution business that will be used to benefit consumers.	We continue to support BEIS and Ofgem on capacity market policy development and applicant readiness. We also continue to work with our delivery partners to achieve operational milestones.	Reducing greenhouse gas emissions forms part of the Company's KPIs (see page 12). We are working with customers and stakeholders to gather insights on the future role of gas in managing the transition to a low-carbon future. We continue to work with BEIS and Ofgem on the development of future energy systems as we respond to the shift to low-carbon energy in the UK.

Our business model

Our business

Our transmission business operates as a regulated monopoly. We have one regulator, Ofgem, who safeguard customers' interests by setting the level of charges we are allowed to pass on and the standards of performance we must achieve.

As System Operator we make sure that supply and demand are balanced in real-time and we facilitate the connection of assets to the transmission system.

The foundations of our business model

Our people and our culture

Our business is built by our people. We work hard to make sure that we keep them as safe as possible. We have nearly 2,000 people working in National Grid Gas.

Being a responsible business

Doing the right thing is a responsibility we take seriously. Being a responsible and sustainable business is fundamental to the way we work and how we manage our impact on the communities in which we operate.

Our relationships with stakeholders and regulators

We engage widely in debate that helps guide future energy policy direction. We work with Ofgem to help them develop the frameworks within which we can meet the changing energy needs of the communities we serve.

Our customer focus

Our customers' wants and needs are evolving with a greater desire to manage their energy use and expectations of how we interact with them. To remain relevant to our customers, we must understand and respond to their changing values and deliver outstanding experiences, products and services.

Innovation

Thinking differently and challenging the norms allow our people to develop innovative and more efficient ways of delivering our services and maintaining our networks.

Our financial capital and fixed asset base

The way in which our investment is funded is an important part of our business. National Grid plc has long-term sustainable assets and strong credit ratings, meaning we are able to secure efficient funding from a variety of sources.

How we generate value

We are a long-term, asset-based business. Our operations are regulated, which means we create value for our stakeholders through predictable revenue streams and cash flows.

Revenue

The vast majority of our revenues are set in accordance with our regulatory agreements, and are calculated based on a number of factors, including:

- performance against incentives;
- deprecation of regulated assets; and
- return on equity and costs debt.

See pages 3 to 5 for more information about our regulatory agreements in the UK.

Cash flow

Our ability to convert revenue to profit and cash is important. By managing our operations efficiently, safely and for the long term, we are able to generate strong sustainable cash flows to finance returns through dividends but also to provide funds for growth.

Investment

We invest efficiently in our networks to deliver strong and sustainable growth in our regulated asset base over the long term.

We continually assess, monitor and challenge investment decisions in order to allow us to continue to a deliver safe, reliable, and cost-effective network.

Our business creates value for our stakeholders in both financial and non-financial terms. Our KPIs benchmark our performance of each of these key areas as shown below.

KPIs Benchmark

Stakeholder	How we generate value	Our measures of success
Stakeholders and communities	Operating as safely, reliably and sustainably as possible; Focusing on affordability to reduce the impact on customer bills; Delivering essential services, while managing loss of supply and customer service issues in a timely way; and Aiming to improve customer satisfaction at all times.	Operating excellence/safety Network reliability Greenhouse gas emissions Customer satisfaction
People	Paying them a market competitive wage, and an overall pay package that rewards competency and performance; and Providing an inclusive culture and encouraging development and employee enablement.	Employee engagement index Workforce diversity
Shareholder	Making sure our regulatory frameworks maintain an acceptable balance between risk and return; Operating within our regulatory frameworks as efficiently and compliantly as possible; Performing well against our regulatory incentives, so we can make the most of our allowed returns; Careful cash flow management and securing low-cost funding; and disciplined investment in our networks and protecting our reputation.	Return on equity Regulated asset base growth

Our people

National Grid Gas plc is a subsidiary of the National Grid plc Group, and its policies and activities contribute to the larger National Grid position. The below represents activities which National Grid Gas plc has contributed to as part of National Grid's achievements in 2016/17.

Building skills and expertise to drive performance

Our sector is undergoing a period of massive transformation and uncertainty, so we are taking steps to help make sure our workforce capacity and capability remains flexible enough to deliver our strategic objectives. For example, we are using a new strategic workforce planning programme. This helps us determine where we could have future shortfalls in our workforce requirements across a range of possible scenarios over the next 10 years. It also helps us plan investment for recruitment and training, so we can make sure we always have the right skills in the right place at the right time.

During 2016/17, we have taken steps to improve our people's capability, primarily across four main areas: leadership, contract management, stakeholder management and performance excellence. We are also setting the standards that we need to achieve in other capability areas, including data management, customer focus and commerciality.

Our Accelerated Development Programme is designed to enhance our leadership succession planning by developing the skills of employees seen as having potential to grow into our senior roles. During 2016/17, 117 participants started the 18-month programme.

Safeguarding the future

We remain committed to helping address the significant skills challenge facing the engineering profession.

The 2015 Employer Skills Survey highlighted that 36% of hard-to-fill vacancies in the UK energy and utilities sector were due to a lack of proficient skills – well above the 23% national average and notably higher than any other sector.

To help address this, we are involved in a number of initiatives. For example, our Chief Executive and specialists from our Academy are members of the Energy and Industrial Partnership Council and Delivery Board and have supported the creation of the Energy and Utilities' Workforce Renewal Skills Strategy 2020. This has involved collaborating with the wider sector to address priorities such as recruitment, investment in skills and targeting skills gaps.

Our Academy offers residential work experience programmes for 100 young people annually, balanced 50/50 between boys and girls. We participate in the annual Big Bang Fair, which is designed to promote interest in Science, technology, engineering and math (STEM) subjects and careers.

During 2016/17, more than 316 people have participated in our apprentice, engineering, student and graduate development programme. In November 2016, our apprentice programmes was ranked 'Outstanding' by Ofsted for the third time consecutively.

Promoting an inclusive and diverse workforce

Our inclusion and diversity activities include attraction and recruitment, development, leadership, role modelling and cultural change.

We aim to attract a diverse range of applicants, including under-represented groups. Our Women in National Grid Yearbook, which showcases a number of our UK female role models, is available to potential applicants so they can envisage a career with us.

We recognise the value that a diverse workforce and an inclusive culture bring to our business. Our policy is that people with disabilities should have fair consideration for all vacancies against the requirements for the role. Where possible, we make reasonable adjustments in job design and provide appropriate training for existing employees who become disabled. We are committed to equal opportunity in recruitment, promotion and career development for all employees, including those with disabilities, and our policy recognises the right of all people to work in an environment that is free from discrimination.

We have reviewed some of our leadership development programmes to place a stronger emphasis on inclusion and diversity. For example we have further developed our unconscious bias training.

We believe leadership involvement is an important factor in building an inclusive culture. Many leaders are sponsors of our employee resource groups or mentees in our reverse mentoring programme. These activities provide our leaders with a greater understanding of the challenges facing our diverse workforce, and more confidence in discussing diversity in the organisation. Senior role models are being encouraged to show how they are bringing an inclusive culture to life.

Our Employee Resource Groups build awareness and understanding of inclusion and diversity throughout the organisation. They also provide valuable feedback and suggestions for improvements. For example, 'One', our ethnic minority group, organised Black History Month events to raise the profile of ethnic diversity.

Our EmployAbility scheme, which provides supported work experience for young people with learning disabilities, is recognised as best practice by the Business Disability Forum.

Following the UK Gender Pay Gap Information Regulations, approved by Parliament in February 2017, we will be disclosing additional pay gap information during 2017 according to the approach outlined in the regulations.

The table below shows the breakdown in numbers of employees by gender at different levels of the organisation. We have included information relating to subsidiary directors, as this is required by the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations 2013. We define 'senior management' as those managers who are at the same level, or one level below, our Executive Committee. It also includes those who are directors of subsidiaries, or who have responsibility for planning, directing or controlling the activities of the Company, or a strategically significant part of the Company, and are employees of the Company.

	Financial year ending 31 March 2017				
	Male	Female	Total	% Male	% Female
Our Board	4	4	8	50	50
Senior Management	30	13	43	70	30
Whole Company	1,286	639	1,925	67	33

Health and well-being

During 2016/17 we have continued to promote the importance of well-being across our business. We have a leading role in the Business in the Community Workwell campaign, which promotes mental well-being in the workplace. More than 900 people, including around 30 of our senior leaders, have attended our mental health first aid course to date. We also ran a diabetes awareness campaign in which employees could assess risk and learn more about diet and activity.

Building strong communities

We believe a strong community is good for the people who live there, good for our business and good for the wider economy. To further support the communities in which we work and live, we partner with charity organisations, provide communities with one-off grants to support their social, economic and environmental development. We also empower our employees to pursue projects and their chosen causes through volunteering in their neighbourhoods.

We support local schools and colleges with work experience opportunities and careers advice sessions. Our engineers help to bring STEM subjects to life. Our engineers help to bring STEM subjects to life. Last year, our community engagement and investment in education was valued at £5,850,965, with our UK employees giving over 18,400 hours of volunteering support.

Human rights

National Grid does not have a specific policy relating to human rights, but respect for human rights is incorporated into our employment practices and our values.

Internal control and risk management

The National Grid Gas Board is committed to protecting and enhancing our reputation and assets, while safeguarding the interests of our stakeholders. It has overall responsibility for the Company's system of risk management and internal control.

Managing our risks

National Grid Gas is exposed to a variety of uncertainties that could have a material adverse effect on the Company's financial condition, our operational results and our reputation.

The National Grid Gas Board oversees the Company's risk management and internal control systems. As part of this role, the Board sets and monitors the amount of risk the Company is prepared to seek or accept in pursuing our strategic objectives (our risk appetite). The Board assesses the Company's principal risks and monitors the risk management process through risk review and challenge sessions twice a year.

Risk management process

Overall risk strategy, policy and process are set at the Group level by National Grid plc with implementation owned by National Grid Gas. Our enterprise risk management process provides a framework through which we can consistently identify, assess and prioritise, manage, monitor and report risks. The process is designed to support the delivery of our purpose, vision, strategy and values, as described on page 10.

Risk management activities occur through all levels of National Grid plc, including National Grid Gas. Through a 'top down, bottom up' approach, all business functions identify the main risks to our business model and to achieving their business objectives. They assess each risk by considering the financial and reputational impacts, and how likely the risk is to materialise. They identify and implement actions to manage and monitor those risks and assess the adequacy of our existing risk controls. The identified risks and actions are collated in risk registers and reported at functional and regional levels of both the Company and the National Grid Group.

An important feature of our risk management process is our three lines of defence model. Each business function owns and is responsible for managing its own particular risks (the first line of defence). A central risk management team (the second line of defence) acts as an advisory function on implementing the risk process and also provides independent challenge of the principal risk assessments and actions taken to mitigate and manage those risks. This team partners with the business functions through nominated risk liaison staff members and collaborates with assurance teams and specialists, such as the safety and compliance management teams to evaluate gaps in controls, identify performance trends and provide recommendations for improvements. National Grid plc's internal audit function then audits selected controls to provide independent assessments of the effectiveness of our risk management and internal control systems (the third line of defence).

Regional senior management regularly reviews and debates the outputs of the bottom-up risk management process. This helps ensure the business is aligned to the Company's strategic objectives and that the prioritisation of the principal risks is discussed regularly. The most significant risks for business are highlighted in risk profiles and reported to the CEO of National Grid plc.

We develop our main strategic uncertainties or 'principal risks' for the Company through input from National Grid plc's Board and the UK Executive Committee and they are determined by the National Grid Gas plc Board. Our risk profile is reported and debated with the UK Executive Committee and National Grid Gas Board every six months. Workshops are held with business leadership teams so we can make sure the principal risks remain closely aligned to our strategic aims and that no significant risks (or combination of risks) are overlooked.

The National Grid Gas Board and leadership teams also discuss the results of testing our principal risks. The aim of this testing is to establish the impact of the principal risks on the Company's ability to continue operating and meet its liabilities over the assessment period. We test the impact of these risks on a reasonable worst case basis, alone and in clusters, over a five-year assessment period. This work informs the viability statement (see page 23).

The outcomes from each level of the risk review process are fed back to the relevant teams and incorporated as appropriate into the next cycle of our ongoing risk process.

The National Grid Gas Audit Committee reviews and reports to the Board on the adequacy and effectiveness of the procedures for the identification, assessment and reporting of business risks, as well as wider internal control, risk management and ethics and compliance matters. As part of its review, the Audit Committee also considers the annual corporate audit plan and any findings raised by the corporate audit function.

Our principal risks

Accepting that it is not possible to identify, anticipate or eliminate every risk that may arise and that risk is an inherent part of doing business, our risk management process aims to provide reasonable assurance that we understand, monitor and manage the main uncertainties that we face in delivering our objectives. This includes consideration of inherent risks, which exist because of the nature of day-to-day operations in our industry, and financial risks, which exist because of our financing activities. Our principal risks and a summary of management and mitigation actions are provided in the table on the following page.

Our corporate risk profile contains the principal risks that the National Grid Gas Board considers to be the main uncertainties currently facing the Group as we endeavour to achieve our strategic objectives. Following the referendum vote for the UK to leave the EU and the consequential uncertainties in the political and economic environment, the Financial Reporting Council (FRC) has highlighted certain specific matters for Boards to consider. In relation to principal risks, the FRC states that boards must consider the nature and extent of risks and uncertainties arising from the result of the referendum and the impact on the future performance and position of the business. Consequently, risk owners have considered Brexit in their assessments of the principal risks. These assessments continue as we gain more clarity on the likely impact of Brexit on our business. Our principal risks are shown in the table below.

Risk area	Risk description	Example of mitigations
Growth	Failure to identify and execute the right opportunities to deliver our growth strategy. Failure to grow our core business and have viable options for new business over the longer term would adversely affect the Company's credibility and jeopardise the achievement of intended financial returns. Our ability to achieve our ambition for growth is subject to a wide range of external uncertainties, including the availability of potential investment targets and attractive financing and the impact of competition for onshore transmission; and internal uncertainties, such as the performance of our operating businesses and our business planning model assumptions.	Processes and resources are in place to review, undertake due diligence and progress new investment opportunities, dispose of existing businesses and identify and execute on opportunities that provide organic growth. These processes, along with twice-yearly Board strategy offsite discussions, are reviewed regularly to ensure they remain supportive of our short- and long-term strategy. We regularly monitor and analyse market conditions, competitors and their potential strategies, the advancement and proliferation of new energy technologies, and the performance of our portfolio. While good progress has been made this past year, we must remain focused on increasing development opportunities in our core business and emerging opportunities. Mitigating actions focus on building our business development pipeline and our capability to pursue non-organic growth options.
Energy policy	Failure to secure satisfactory regulatory outcomes and to influence future energy policy. Policy decisions by regulators, governments and others directly affect our business. We must engage widely in the energy policy debate, making sure our position and perspective help to shape future policy direction.	We strive to maintain a good understanding of the regulatory agenda and emerging issues, so that robust, public interest aligned responses can be selected and developed in good time. Our reputation as a competent operator of important national infrastructure is critical to our ability to do this. As part of our new business strategy, we have renewed our stakeholder engagement strategy to improve focus on business objectives. The new strategy incorporates senior executive ownership of each priority, and the development of key positions and engagement plans by cross-functional teams.

Risk area	Risk description	Example of mitigations
Emerging technology	Failure to effectively respond to the threats and opportunities presented by emerging technologies, particularly adapting our networks to meet the challenge of increasing distributed energy sources. Technology developments in areas such as solar energy, energy storage and distributed generation have developed at a faster pace than many anticipated. We face the challenge of adapting our networks to meet new demands as well as ensuring we act on the opportunities that will benefit our customers and stakeholders.	We created a technology team within our Strategy function to develop relationships with emerging and technology-centric organisations, to monitor disruptive technology and business model trends and to act as a bridge for emerging technology into the core regulated businesses and business development teams.
Safety	Catastrophic asset failure resulting in a significant safety event. Safety is a fundamental priority. Some of the assets owned and operated by National Grid Gas are inherently hazardous and process safety incidents, while extremely unlikely, can occur. Our objective is to be an industry leader in managing the process safety risks from our assets to protect our employees, contractors and the communities in which we operate. We operate in compliance with regional legislation and regulation. In addition, we identify and adopt good practices for safety management.	We continue to commit significant resources and financial investment to maintain the integrity of our assets and we strive to continuously improve our key process safety controls. Our Company-wide process safety management system is in place to ensure a robust and consistent framework of risk management exists across our higher hazard asset portfolio. We have a mature insurance strategy that uses a mix of self-insurance, captives and direct (re)insurance placements. This provides some financial protection in respect of property damage, business interruption and liability risks. Periodically, independent surveys of key assets are undertaken, which provide risk engineering knowledge and best practices to the Company with the aim of further reducing our exposure to hazard risks.
Data management	Failure to operate with a sufficiently mature business data management capability. The need for accurate, timely, and meaningful data lies throughout the organisation and is critical to our core processes and our ability to grow the business. We must rely upon the performance of our systems and data to demonstrate the value of our business to our stakeholders, meet our obligations under our regulatory agreements and comply with agreements with providers of finance.	We have developed data management principles and minimum standards with supporting guidelines. These documents provide clarity around what is expected, with a strong focus on what we need in place to keep us safe, secure and legally compliant. These standards have been launched in the business and will form part of the Business Management System that will be developed in the coming year. In support of this, we are also developing a capability framework, to make sure our people have the appropriate skills and expertise in data management. The businesses will continue to develop their own implementation plans against these new standards and capabilities. The aim of these plans will be to ensure we can demonstrate we are compliant with the minimum standards and have the core capabilities in place for all of our business critical data. To support these efforts, we are establishing a regional centre of excellence for data management. Their role will be to provide expertise to the businesses and to help provide assurance around the effectiveness of the data management standards.

Risk area	Risk description	Example of mitigations
Cyber breach	We experience a major cyber security breach of business and Critical National Infrastructure (CNI) systems. Due to the nature of our business we recognise that our CNI systems may be a potential target for cyber threats. We must protect our business assets and infrastructure and be prepared for any malicious attack.	We use industry best practices as part of our cyber security policies, processes and technologies. Our cyber security programme is a global programme of work which started in 2010 and continues to be modified and updated to this day. This programme is intended to reduce the risk that a cyber-threat could adversely affect the Company's business resilience. We continually invest in cyber strategies that are commensurate with the changing nature of the security landscape. This includes collaborative working with BEIS and the Centre for Protection of National Infrastructure on key cyber risks and development of an enhanced CNI security strategy. We also collaborate with a number of regulatory agencies focused on protection of CNI.
Leadership capacity	Failure to build skills and leadership capacity (including effective succession planning) required to deliver our vision and strategy. It is through the high-quality work of our employees that we will achieve our vision, respond to the changing needs of our stakeholders and create a competitive advantage. Obtaining and fostering an engaged and talented team that has the knowledge, training, skills and experience to deliver on our strategic objectives is vital to our success. We must attract, integrate and retain the talent we need at all levels of the business.	Strategic workforce planning allows us to effectively inform our strategic resourcing plans. Our entry level talent development schemes (graduate training and apprenticeships) are a potential source of competitive advantage in the market place. We are involved in a number of initiatives to help secure the future engineering talent required. Improvements to our talent processes mean we continue to improve in identifying talent and in accelerating development of future leaders (e.g. our Accelerated Development Programme). The rigour of our succession planning and development planning process has been improved, particularly at senior levels and is now being applied deeper into the organisation. In all strategies and programmes we continue to promote inclusion and diversity. To help understand our workforce, we formally solicit employee opinions via a Company-wide employee survey that is conducted annually.

Our internal control process

We have a number of processes to support our internal control environment. These processes are managed by dedicated specialist teams, including risk management, ethics and compliance management, corporate audit and internal controls, and safety, environment and health. Oversight of these activities is provided through regular review and reporting to the Board and appropriate Board committees as outlined in the Corporate Governance section on pages 29 to 36.

Monitoring internal control is conducted through established boards and committees at different levels of the National Grid plc organisation. Deficiencies are reported and corrected at the appropriate entity-level. The most significant risk and internal controls issues are monitored at the Senior Executive and National Grid plc Board level. The Audit Committee is responsible for keeping under review and reporting to the Board on effectiveness of reporting, internal control policies, Bribery Act legislation, appropriateness of financial disclosures and procedures for risk and compliance management, business conduct and internal audit.

Reviewing the effectiveness of our internal control

Each year the National Grid Gas Board reviews the effectiveness of our internal control systems and risk management processes covering all material systems, including financial, operational and compliance controls, to make sure they remain robust.

The latest review covered the financial year to 31 March 2017 and the period to the approval of this Annual Report and Accounts. In this review, the National Grid Gas Board considered the effectiveness of areas such as the control environment, risk management and internal control activities, including those described below.

Fostering a culture of integrity is an important element of our risk management and internal controls system. National Grid Gas's values – 'do the right thing' and 'find a better way' - provide a framework for reporting business conduct issues, educating employees and promoting a culture of integrity at all levels of the business. We have policies and procedures in place to communicate behaviour expected from employees and third parties, and to prevent and investigate fraud and bribery and other business conduct issues. We monitor and address business conduct issues through several means, including a biannual review by the Audit Committee.

Overall compliance strategy, policy and frameworks are set at the National Grid plc Group-level with implementation owned by National Grid Gas. The business is responsible for identifying compliance issues, continuous monitoring, and developing actions to improve compliance performance. We monitor and address compliance issues through several means including reviews at leadership meetings and a biannual review by the Audit Committee.

The Certificate of Assurance (CoA) from the CEO to the Board provides overall assurance around the effectiveness of our risk management and internal controls systems. The CoA process operates via a cascade system and takes place twice-yearly in support of the financial end of year review and half-year review.

The periodic reports on management's opinion on the effectiveness of internal controls over financial reporting are received by the National Grid Gas Audit Committee and Board in advance of the half- and full-year results.

The National Grid Gas Board evaluated the effectiveness of management's processes for monitoring and reviewing internal control and risk management. It noted that no material failings or weaknesses had been identified by the review and confirmed that it was satisfied the systems and processes were functioning effectively.

Our internal control and risk management processes comply with the requirements of the UK Corporate Governance Code.

Internal control over financial reporting

We have specific internal mechanisms that govern the financial reporting process and the preparation of the Annual Report and Accounts. Our financial controls guidance sets out the fundamentals of internal control over financial reporting, which are applied across the Company.

Our financial processes include a range of system, transactional and management oversight controls. In addition, our businesses prepare detailed monthly management reports that include analysis of their results, along with comparisons to relevant budgets, forecasts and prior year results. These are presented to, and reviewed by, senior management within our Finance function.

These reviews are supplemented by quarterly performance reviews, attended by the CEO and CFO. The reviews consider historical results and expected future performance and involve senior management from both operational and financial areas of the business.

Viability statement

The Board's consideration of the longer-term viability of the Company is an extension of our group wide business planning process, which includes financial forecasting, a robust risk management assessment, regular budget reviews and scenario planning. Our business strategy aims to make sure that our operations and finances are sustainable.

National Grid Gas plc (NGG) is a wholly owned subsidiary of National Grid Plc which performed a group wide business plan that was reviewed and approved by the National Grid plc Board and which included sufficient detail of the NGG operating segment.

Given our business model, current regulatory clarity, other factors impacting our operating environment, and the robustness of our business planning process, the Board have concluded that five years is the most appropriate timeframe over which to assess the long-term viability of the Company. This is in line with our five year business plan and one year budget which are reviewed and approved by the National Grid plc Board.

The business plan considers the significant solvency and liquidity risks involved in delivering our business model in light of our strategic priorities. The business plan models upside and downside scenarios derived from the risks and opportunities identified, and determines the impact these would have on our results and financial position over the five year period. We have set out the details of the principal risks facing our Company on pages 18 to 21, described in relation to our ability to deliver our strategic objectives. We identify our principal risks through a roust assessment that includes a continuous cycle of bottom up reporting and review, and top down feedback.

Our business model calls for continued capital investment to maintain and expand our network infrastructure. To deliver this, our business plan highlights that we may need to access capital markets to raise additional funds from time to time. We have a long and successful history in this regard. Our business plan also models various KPIs used by lenders in assessing a company's credit worthiness. These models indicate that we should continue to have access to capital markets at commercially acceptable interest rates throughout the five year period.

No principal risk or cluster of principal risks was found to impact upon the viability of the Company. Preventative and mitigating controls in place to minimise the likelihood of occurrence and/or financial and reputation impact are embedded within our robust assurance system.

In assessing the impact of the principal risks on the Company, the Board has considered the fact that we operate in stable markets and the robust financial position of the Company, including the ability to sell assets, raise capital and suspend or reduce the payment of dividends. It has also considered Ofgem's legal duty to have regard to the need to fund licenced National Grid Gas plc activities.

Each Director was satisfied that they had sufficient information to judge the viability of the Company. Based on the assessment described above and on page 38, the Directors have a reasonable expectation that the Company will be able to continue operating and meet its liabilities over the period to June 2022.

The Strategic Report was approved by the Board of Directors on 30 June 2017 and signed on its behalf by:

Alan Foster
Director

Financial review

We have delivered another year of solid financial performance. Revenue from continuing operations increased by £101 million to £1,340 million and adjusted operating profit remained consistent at £573 million.

Use of adjusted profit measures

In considering the financial performance of our business and segments, we analyse each of our primary financial measures of operating profit and profit before tax into two components.

The first of these components is referred to as an adjusted profit measure. This is the principal measure used by management to assess the performance of the underlying business. Adjusted results exclude exceptional items and remeasurements. These items are reported as the second component of the financial measures. Note 3 to the consolidated financial statements explains in detail the items which are excluded from our adjusted profit measures.

Adjusted profit measures have limitations in their usefulness compared with the comparable total profit measures as they exclude important elements of our financial performance. However, we believe that by presenting our financial performance in two components it is easier to read and interpret financial performance between periods, as adjusted profit measures are more comparable having removed the distorting effect of the excluded items. Those items are more clearly understood if separately identified and analysed.

The presentation of these two components of financial performance is additional to, and not a substitute for, the comparable total profit measures presented.

Management uses adjusted profit measures as the basis for monitoring financial performance. These measures are also used when communicating financial performance to its investors in external presentations and announcements of financial results.

Internal financial reports, budgets and forecasts are primarily prepared on the basis of adjusted profit measures, although planned exceptional items, such as significant restructurings, are also reflected in budgets and forecasts. We separately monitor and disclose the excluded items as a component of our overall financial performance.

Reconciliations of adjusted profit measures

Reconciliation of adjusted operating profit to total operating profit

Adjusted operating profit is presented on the face of the income statement under the heading operating profit before exceptional items.

Years ended 31 March

Continuing	2017	2016
	£m	£m
Adjusted operating profit	**573**	573
Exceptional items[1]	**(109)**	-
Total operating profit	**464**	573

Reconciliation of adjusted operating profit to adjusted earnings and earnings

Years ended 31 March

Continuing	2017	2016
	£m	£m
Adjusted operating profit	**573**	573
Adjusted net finance costs	**(155)**	(120)
Adjusted profit before tax	**418**	453
Adjusted taxation	**(66)**	(100)
Adjusted profit after tax	**352**	353
Attributable to non-controlling interests	**-**	-
Adjusted earnings	**352**	353
Exceptional items after tax	**(47)**	46
Remeasurements after tax	**(6)**	(7)
Earnings	**299**	392

Reconciliation of adjusted operating profit excluding timing differences to total operating profit

Adjusted profit excluding timing differences is presented below.

Years ended 31 March

Continuing	2017	2016
	£m	£m
Adjusted operating profit excluding timing differences	**511**	506
Timing differences[1]	**62**	67
Adjusted operating profit	**573**	573
Exceptional items [2]	**(109)**	-
Total operating profit	**464**	573

1 Our operating profit for the year includes a total estimated in-year over-collection of £62 million (2015/16: £67 million over-collection).

[2] £109 million gain on the sale of land sites, offset by the creation of £107 million of gas holder demolition provisions, £89 million of costs incurred due to sectionalisation of the National Grid UK Pension Scheme and £22 million of pension deficit charges.

Consolidated income statement commentary

The commentary below describes the continuing business results for the year ending 31 March 2017.

	Years ended 31 March	
	2017	2016
	£m	£m
Revenue	**1,340**	1,239
Operating costs	**(767)**	(666)
Operating profit	**573**	573
Exceptional items	**(109)**	-
Finance income	**5**	1
Finance costs:		
Before exceptional items and remeasurements	**(160)**	(121)
Exceptional items and remeasurements	**(7)**	(9)
Profit before tax	**302**	444
Taxation:		
Before exceptional items and remeasurements	**(66)**	(100)
Exceptional items and remeasurements	**63**	48
Profit after tax	**299**	392

Revenue

Revenue for the year ended 31 March 2017 increased by £101 million to £1,340 million. Following the sale of the Gas Distribution business from the NGG group, £70 million of sales in Gas Transmission to the Gas Distribution business for the period from 1 October 2016 to 31 March 2017 have been classified as external. The increase in revenue is also reflective of increased regulated revenue allowances and higher volumes.

Operating profit

Adjusted operating profit for continuing operations for the year ended 31 March 2017 of £573 million is in line with the prior year.

Exceptional items of £109 million included in our operating costs for the year ended 31 March 2017 relate to £109 million gain on the sale of land sites, offset by the creation of £107 million of gas holder demolition provisions, £89 million of costs incurred due to sectionalisation of the National Grid UK Pension Scheme and £22 million of pension deficit charges.

Net finance costs

For the year ended 31 March 2017, net finance costs before exceptional items and remeasurements of £155 million were £35 million higher than the prior year, principally driven by increase in RPI rates.

Exceptional finance costs for the year ended 31 March 2017 included a loss of £7 million on financial remeasurements, relating to net gains and losses on derivative financial instruments.

Taxation

The tax charge on profits before exceptional items and remeasurements was £34 million lower than 2015/16. This was mainly due to lower profits and adjustments in respect of prior years of £38 million offset by £26 million of expenses not deductible for tax purposes.

Exceptional tax for 2016/17 primarily relates to a £63 million tax charge arising on the exceptional items above.

Consolidated statement of financial position commentary

The consolidated statement of financial position sets out all the Group's assets and liabilities at the year end. As a capital-intensive business, we have significant amounts of physical assets and corresponding borrowings.

	Year end 31 March	
	2017	2016
	£m	£m
Non-current assets	**8,762**	19,547
Current assets	**2,447**	675
Total assets	**11,209**	20,222
Current liabilities	**(1,787)**	(2,789)
Non-current liabilities	**(5,583)**	(10,510)
Total liabilities	**(7,370)**	(13,299)
Net assets	**3,839**	6,923

As at 31 March 2017, the balance sheet no longer includes the assets and liabilities of Gas Distribution (see note 7). The disposal of these assets and liabilities is referred to as 'disposal' in the commentary below.

Property, plant and equipment

Property, plant and equipment decreased by £8,315 million to £4,339 million as at 31 March 2017. This was due to capital expenditure of £500 million on the renewal and extension of our regulated assets, offset by £364 million of depreciation in the year and net disposals of £8,448 million (net disposal on Gas Distribution of £8,431 million).

Other non-current assets

Other non-current assets, which comprises an interest-free loan to our immediate parent company, National Grid Gas Holdings Limited decreased by £2,183 million, and non-current prepayments which decreased by £14 million.

Trade and other receivables

Trade and other receivables have increased by £74 million to £520 million at 31 March 2017. This increase is principally due to an increase in prepayments and amounts owed by fellow subsidiaries of £62 million and £148 million respectively and a decrease in accrued income of £141 million as a result of the disposal.

Derivative financial liabilities

The £147 million decrease in derivative liabilities is mainly due to inflation linked swap terminations as part of restructuring of the NGG portfolio. This is partially offset by a small increase in the value of inflation linked swaps.

Trade and other payables

Trade and other payables have decreased by £205 million to £614 million. This was primarily due to a decrease in trade payables of £205 million linked to the disposal.

Current and deferred tax liabilities

Current tax liabilities of £9 million have decreased from £34 million. The net deferred tax liability decreased by £1,182 million to £366 million, mainly as a result of the disposal of £1,063 million and an increase in accelerated tax depreciation.

Provisions

Provisions (both current and non-current) increased by £105 million in the year. Additions include £107 million for demolition of the non-operational gas holders on sites sold following the sale of Gas Distribution where a constructive obligation was created. A further £138 million of business set up costs and business restructuring costs on the disposal of Gas Distribution have been recognised in the year. These are offset by £94 million from the disposal of the Gas Distribution business and utilisation and releases of £28 million and £23 million respectively.

Other non-current liabilities

Other non-current liabilities decreased by £858 million to £189 million due primarily to deferred income reducing by £870 million on disposal.

Other balance sheet items

During the year ended 31 March 2017 pension sectionalisation occurred within the National Grid plc Group, with the National Grid UK Pension Scheme being split into three parts, Sections A, B and C. National Grid Gas became a sponsoring employer for Section B. This has resulted in a change in National Grid Gas from recognising a pension charge for the year and recognising the scheme as if it were a defined contribution scheme to recognising a net pension asset on the balance sheet and accounting as a defined benefit scheme.

We operate pension arrangements on behalf of our employees the majority of whom are members of the defined benefits section which is closed to new entrants. Membership of the defined contribution section of the National Grid Pension Scheme is offered to all new employees.

Net pensions obligations

A summary of the total assets and liabilities and the overall net IAS 19 (revised) accounting surplus is shown below:

Net scheme (liability)/asset	£m
As at 1 January 2017	(89)
Current service cost	(5)
Net interest cost	(1)
Administration and other	(2)
Actuarial gains	
on plan assets	83
on plan liabilities	51
Employer contributions	8
As at 31 March 2017	45

The principal movements in (liability)/asset during the year include net actuarial gains of £134 million and employer contributions of £8 million. The overall obligation moved by £134 million to a closing asset of £45 million.

Further information on our pensions benefit obligations can be found in notes 19 and 26 to the consolidated financial statements.

Cash flow statement commentary

The commentary below describes the continuing business results for the year ending 31 March 2017.

Cash inflows and outflows are presented to allow users to understand how they relate to the day-to-day operations of the business (operating activities); the money that has been spent or earned on assets in the year, including acquisitions of physical assets or other businesses (investing activities); and the cash raised from debt or share issues and other loan borrowings or repayments (financing activities).

Reconciliation of cash flow to net debt	2017 £m	2016 £m
Cash generated from operations	**723**	729
Net capital expenditure	**(246)**	(223)
Business net cash flow	**477**	506
Net interest paid	**(88)**	(96)
Tax paid	**(30)**	(81)
Dividends paid	**(8,100)**	(620)
Discontinued operations	**7,249**	440
Other	**5,759**	(81)
Net debt decrease	**5,267**	68
Opening net debt	**(8,452)**	(8,520)
Closing net debt	**(3,185)**	(8,452)

Cash generated from operations

Cash flows from our operations are largely stable when viewed over the longer term. Our gas transmission and gas distribution operations are subject to a multi-year price control agreements with Ofgem.

For the year ended 31 March 2017, cash flow from operations decreased by £6 million to £723 million. Changes in working capital decreased by £72 million from the prior year, principally due to movements on intercompany balances with other National Grid companies. Offset by changes in provisions of £65 million.

Net capital expenditure

Net capital expenditure in the year of £246 million was £23 million higher than the prior year.

Dividends paid

National Grid Gas paid two dividends during the year, 'interim dividend A' of £5,917m and 'interim dividend B' of £2,183m, together the interim dividends. The interim dividends were made to ensure partial distribution of the proceeds from the Gas Distribution business. This was £7,480 million higher than 2015/16 (see note 6).

Discontinued operations

The Gas Disposal business contributed £7,249 million to the cash flow in the current year, primarily due to proceeds from the sale and debt restructuring within investing activities of £6,585 million. Cash flows from operations were £460 million and cash flows from financing activities were £204 million.

Other movements in net debt

Other movements in net debt principally include the disposal of £4,051 million of net debt with the Gas Distribution business sale which comprised £4,050 million of borrowings, £4 million of derivative liabilities, offset by £3 million of cash and cash equivalents. In addition, within other movements a £2,183 million cash inflow was received on repayment of an intra group loan, offset by non-cash movements, which includes accretion and other fair value movements.

Regulated financial performance

Timing and Regulated Revenue Adjustments

Our allowed revenues are set in accordance with our regulatory price controls. We calculate the tariffs we charge our customers based on the estimated volume of energy and cost we expect will be delivered during the coming period. The actual volumes delivered will differ from this estimate. Therefore, our total actual revenue will be different from our total allowed revenue. These differences are commonly referred to as timing differences. If we collect more than the allowed level of revenue, the balance must be returned to customers in subsequent periods, and if we collect less than the allowed level of revenue we may recover the balance from customers in subsequent periods.

The amounts calculated as timing differences are estimates and subject to change until the variables that determine allowed revenue are final. Our operating profit for the year includes a total estimated in-year over-collection of £62 million (2015/16: £67 million over-collection). Our closing balance at 31 March 2017 was £113 million over-recovery (2016: over-recovery of £39 million). All other things being equal, the majority of that balance would normally be returned to customers in the year ending 31 March 2019.

In addition to the timing adjustments described above, following the start of the RIIO price controls outperformance against allowances as a result of the totex mechanism, together with changes in output-related allowances included in the original price control, will almost always be adjusted in future revenue recoveries, typically starting in two years' time.

Our current IFRS revenues and earnings will therefore include these amounts that will need to be repaid or recovered in future periods. Such adjustments will form an important part of the continuing difference between reported IFRS results and underlying economic performance based on our regulatory obligations.

Return on Equity

Return on Equity for the year, using a long-run inflation rate of 3%, was 10.8% compared with a regulatory assumption, used in calculating the original revenue allowance, of 10.0%. The principal components of the difference are shown in the table below.

Year ended 31 March	**2017**	2016
Base return (including avg. 3% long-run inflation)	**10.0%**	10.0%
Totex incentive mechanism	**(0.8)%**	(0.2)%
Other revenue incentives	**1.1%**	1.2%
Return including in year incentive performance	**10.3%**	11.0%
Pre-determined additional allowances	**0.5%**	1.5%
Return on Equity	**10.8%**	12.5%

The business performed below the targets set by the totex incentive mechanism in the fourth year of RIIO. Totex spend was £351m, compared to an estimated allowance, adjusted for outputs and phasing of £312m. Performance reflected higher asset health spend and a small reduction in allowances reflecting the outcome of the MPR. The Company's share of this difference is expected to be £17m.

The business had another good year of incentive performance, just below the performance levels in 2015/16. Increased efforts to identify customer and stakeholder needs were offset by lower shrinkage performance. Overall, the Gas Transmission business delivered around 110 bps of additional returns through other revenue incentives. On a pre-tax basis, this equates to an estimated £29m of additional revenue allowance, most of which is due to be recovered in future years under the RIIO funding mechanisms.

Contribution from legacy incentives was 50bps, a decrease year-on-year, as expected and in accordance with the agreed profile.

Regulated Financial Position

RAV increased 3% in the year reflecting the impact of inflation and continued investment, partially offset by depreciation and adverse performance RAV. Net other regulatory assets decreased by £120m, mainly reflecting current year revenue over recoveries associated with lower than expected inflation and higher volumes.

£m	**2017**	2016
Opening Regulated Asset Value (RAV)*	**5,597**	5,525
Asset additions (aka slow money) (actual)	**201**	185
Performance RAV or assets created	**(11)**	(5)
Inflation adjustment (actual RPI)	**175**	85
Depreciation and amortisation	**(207)**	(196)
Closing RAV	**5,755**	5,594
Opening balance of other regulated assets and (liabilities)*	**56**	157
Movement	**(120)**	(80)
Closing balance	**(64)**	77
Closing Regulated Financial Position	**5,691**	5,671

*2016/17 opening balances adjusted to correspond with 2015/16 regulatory filings and calculations

Discontinued operations

Discontinued operations comprise the Gas Distribution and Xoserve businesses. The results of the discounted operations are presented below:

	Years ended 31 March	
	2017	2016
Discontinued operations	**£m**	£m
Revenue	**927**	1,913
Operating costs	**(531)**	(1,056)
Operating profit	**396**	857
Net finance costs	**(77)**	(115)
Profit before tax	**319**	742
Taxation	**(5)**	(25)
Profit after tax	**314**	717
Gain on disposal	**4,024**	-
Taxation on gain on disposal	**213**	-
Gain on disposal	**4,237**	-
Total	**4,551**	717

Operating profit for discontinued operations decreased by £461 million to £396 million. Revenue was £986 million lower, reflecting the sale of the businesses half way through the financial year.

The net gain on disposal includes net consideration of £7,561 million less financing costs of £833 million and transaction costs of £261 million.

Costs included in the gain on disposal total £1,094 million. These include the direct costs of selling Gas Distribution ('transaction costs') and the costs for activities undertaken to prepare and structure the disposal ('business set-up costs'). The gain on disposal totalled £4,237 million.

Corporate Governance

Corporate Governance Statement

National Grid Gas aims to achieve high standards of leadership and governance. At the National Grid level, its Board considers that it complied in full with the provisions of the UK Corporate Governance Code 2014 (the Code) during the year being reported on. National Grid Gas is not required to comply with the Code; however, the Board is mindful of the principles of the Code and develops its governance and oversight of the Company considering not only its ultimate shareholder, National Grid, but the wider range of stakeholders in its business. The Corporate Governance Statement sets out the principal areas of Board governance together with an explanation of areas where it considers that it has operated consistently with the main principles of the Code.

Governance framework

The Board of the Company is collectively responsible for its governance, and oversees its effective oversight of the Company and its businesses, and compliance with all relevant laws and regulations, including compliance with its obligations under its Gas Transporter Licences. To facilitate this, a comprehensive governance framework has been established. This governance framework forms part of the wider National Grid plc governance framework and is aligned, as required and is applicable, to the Company. Risk management is fundamental to delivering the long term success of the Company and for that reason a separate section of this Annual Report and Accounts has been dedicated to describing our internal controls and risk management, see page 18. The day-to-day operational and financial management of the Company's businesses is undertaken by committees. The committees are operated in compliance with business separation obligations set out in its licenses.

2016/17 – A year of change

During this financial year the Board oversaw the separation of the Gas Distribution business from its operations into a separate legal entity (National Grid Gas Distribution Limited ("NGGD")) in preparation for the sale of a majority stake in the Gas Distribution business by National Grid plc. The separation process required oversight and sound governance principles to be applied throughout a complex transaction delivered under tight timescales. Focus on the Company's ongoing business, both before and post the separation of the Gas Distribution business, was maintained through the diligent governance principles of leadership, effectiveness and accountability that have been embedded in the way the Board operates. Further details on how this was achieved can be found in the sections that follow.

Reinforcing its commitment to sound corporate governance the Board has continued to strengthen and develop both its composition and governance framework, implementing, as applicable, many of the best practice governance principles in operation at the National Grid plc level.

Board composition

The Board consists of six executive directors and two Sufficiently Independent Directors ("SIDs") who between them provide a broad and diverse range of experience and technical skills from both within and external to the organisation, from the energy sector, other regulated industries and external bodies. This depth and breadth of experience, and the independence brought by the SIDs, enables the Board to engage in constructive and challenging discussions, considering the perspectives and interests not only of the Company's shareholder but the wider range of stakeholders in the business. Details of the director positions, demonstrating their area of responsibility within the business, can be found under the section "How our Board operates".

Last year we reported on the change in Board composition resulting from internal changes in executive director roles. During this year the Board has consolidated its composition under the leadership of the new Executive Director, UK, Nicola Shaw CBE, who became Chairman of the Board in July 2016. Nicola also sits as an Executive Director on the National Grid plc Board. Through her participation at the Boards of both companies, the Board of National Grid Gas is well placed to identify and facilitate understanding of the views of its ultimate shareholder.

Sufficiently Independent Directors

The appointment of two Sufficiently Independent Directors (SIDs) in April 2014 has provided the Board with independent challenge and input to the decision making process. The SIDs bring to the Board a wealth of experience and knowledge derived from working in other businesses in the utility sector, government and regulatory organisations and other businesses and organisations outside of the energy sector. Dr Clive Elphick and Dr Catherine Bell have remained in these roles providing continuity, and an independent voice in the boardroom, during a period of internal change. Their input and involvement in developing the governance framework is demonstrated through their leadership of two committees of the Board: the Audit Committee and Business Separation Compliance Committee. Within the boardroom, the constructive independent challenge and input brought by the SIDs, supports the Board in considering the wider range of stakeholders in the business. Outside of the boardroom, the SIDs hold an annual meeting with the Chief Executive Officer of National Grid plc, enabling them to strengthen their, and the Board's, engagement and understanding of the views of the shareholder. Additionally, in their roles as members of the Company's Audit Committee, the SIDs hold an annual meeting with the Chair of the National Grid plc Audit Committee creating a formal information flow between the independent directors of the two committees.

The SIDs attend a range of site and operational visits throughout the year, enabling them to strengthen their knowledge and understanding of the business and current operational matters. These visits also provide the opportunity to create further links between the business and the Board room.

Executive Directors

The executive director membership of the Board consists of the senior managers of the gas transmission and system operator businesses, regulatory function and financial function.

During the year the Board's executive director composition changed following the retirement of Mark Ripley, Director UK Regulation. Chris Bennett was appointed to this role and accordingly appointed to the Board in June 2016.

The separation of the Gas Distribution business on the 1 October 2016 saw the departure of executive directors Chris Train and Julian Allsopp, directors who specifically represented the Gas Distribution business on the Board.

All Board appointments are made in consultation with its shareholder and in accordance with National Grid's Procedure for the Appointment of Directors to Subsidiary Companies.

Director induction and development

Director training on the statutory duties and responsibilities of directors has been made available to new and existing directors and reference material has been placed in the online document library.

As part of the induction process, internal personnel are requested to attend the Board meeting immediately prior to their appointment, to facilitate familiarisation with the Board members and governance framework and procedures.

Continuing director training and development is delivered both within and outside of the boardroom. A programme of head office and operational site visits, briefings and internal conferences and events aims to strengthen and refresh the Board's knowledge and understanding of the Company's operations, the external business and regulatory environment and specific technical briefings to support the directors in fulfilling their roles on both the Board and Board Committees. The visits and briefings provide an opportunity for the directors to support and reinforce the Company's culture, values and ethics and promote a culture of openness between Board members and employees and add depth and knowledge to the discussions in the boardroom.

Within the boardroom, the Board receive updates and presentations on current operational matters and specific initiatives within the business and wider National Grid group. These presentations also provide an opportunity for the individual executive directors to benefit from the input of other Board members on matters within their area of the business.

How our Board operates

The Board maintains a schedule of matters specifically reserved for its consideration and decision. This is aligned, as appropriate, to that of the National Grid plc board with additional responsibilities as required by licence obligations. The matters reserved cover matters categorised as: Strategy, Management and Finance, Director and Employee Issues, Corporate Governance, Financial and Regulatory Reporting and Shareholders and includes oversight of the relationship with the regulatory bodies, including Ofgem, Department of Energy and Climate Change (now part of the Department for Business, Energy and Industrial Strategy) and the Health and Safety Executive.

To support the Board, there is an established framework of Committees, to which the Board delegates defined duties under Terms of Reference and within a framework of Delegations of Authority. Further detail on the work of the Committees can be found below.

The Board's accountability for financial and business reporting and risk management and internal control is undertaken within the wider Group governance framework and processes. As a regulated entity, the Board has responsibility for the annual regulatory accounts to which it applies the same rigorous governance processes as that of the statutory accounts, and it involves the work of the Audit Committee. Reporting on the regulatory regime is overseen by the Board, and further detail can be found in the section "What we do – Regulation".

Board meetings are scheduled and communicated a minimum of one year in advance providing all directors with sufficient notice to attend meetings. The matters to be considered throughout the annual board meeting schedule fulfil the Board's responsibilities in line with its statutory duties, licence obligations, its matters reserved for the Board and its authority under the Group Delegations of Authority from National Grid plc. The Board's supervision of the Company's operations is fulfilled through standing agenda items on health and safety matters, business overviews from the transmission owner and system operator and financial performance. The Board's consideration of health and safety matters covers all parts of the operational business and takes into account the health and safety of both employees and the public. In addition to this the Board receives a suite of management reports, in line with Group reporting, providing updates on different aspects of the business.

In its steering role, providing leadership to the business, the Board receive papers requesting their input and decision on matters, aligned to the matters reserved to it. The Board regularly reviews the annual business schedule, and amends this to take account of changes in the external and internal environment, enabling it to provide effective, time appropriate leadership and oversight of matters affecting the business.

To enable the Board to be effective and efficient within the boardroom a number of procedures have been established: papers supporting each agenda item are distributed in advance, typically a week before the meeting; training and briefings on specific matters are scheduled prior to the board meeting; a 'Safety Moment' is presented at each Board Meeting, which considers ongoing initiatives and activities both within the business and externally; and the Chairman holds a short meeting with the SIDs, before each meeting to discuss the focus of the upcoming meeting. After each meeting the Chairman and SIDs meet to share feedback and discuss the dynamics of the meeting, enabling a process of continuous improvement for the operation of future board meetings.

The separation of the Gas Distribution business was overseen by the Board consistently applying the embedded governance processes and procedures it has in place, providing leadership and direction throughout the separation process. Additional time was allocated within the scheduled board meetings for separate agenda items on the specific requirements and impacts of separating the Gas Distribution business in preparation for sale. These were supported by the project director for the sale of the Gas Distribution business. The Board consistently considered the impact on the retained business and the separated business throughout the separation process.

In addition to the discussions during scheduled board meetings, a programme of additional Board and Audit Committee meetings, supplemented by technical briefings, were held to enable the Board to provide appropriate focus on the specific requirements of them in relation to the separation process. These additional meetings and briefings were attended by specialist National Grid employees who were members of the National Grid project team managing the sale of the Gas Distribution business. To provide the Board with support on the technical, financial, legal and regulatory aspects of the separation process, briefings were delivered by internal specialists and external advisers engaged on the sales process.

Board performance evaluation

Following the externally facilitated board evaluation in June 2015, progress against the actions has continued, developing and enhancing the performance of the Board. The developments and enhancements are demonstrated throughout this corporate governance report, as we report on the various areas of increased rigour around the Company's corporate governance procedures and practices.

The value of the board evaluation process, and subsequent progress against the actions, has been demonstrated through the Board's successful focus throughout the year on ongoing leadership of the business whilst overseeing the requirements of the separation of the Gas Distribution business.

Board membership and attendance

Six Board meetings were scheduled and held during the last financial year. Board membership and attendance at the meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2017.

		Attendance
Nicola Shaw CBE (Chair) [1]	Executive Director UK	4 of 4
Chris Murray (Chair) [2]	Chair of the Board	2 of 2
Andy Agg	Group Tax & Treasury Director	5 of 6
Alan Foster	UK CFO	5 of 6
Pauline Walsh	Director Gas Transmission Owner	6 of 6
Cordi O'Hara	Director of UK System Operator	4 of 6
Chris Bennett [3]	Director UK Regulation	5 of 5
Mark Ripley [4]	Director UK Regulation	1 of 1
Chris Train [5]	Director Gas Distribution	1 of 3
Julian Allsopp [6]	Financial Controller Gas Distribution	3 of 3
Catherine Bell	Sufficiently Independent Directors	6 of 6
Clive Elphick	Sufficiently Independent Directors	6 of 6

1. Appointed 27 July 2016
2. Resigned 27 July 2016
3. Appointed 25 June 2016
4. Resigned 24 June 2016
5. Resigned 1 October 2016
6. Resigned 1 October 2016

For those meetings where an executive Director was unable to attend, alternative arrangements were put in place to ensure the Board had representation from the relevant functional area. This was either through the attendance of a senior manager from within the applicable functional area or a written briefing provided by the Director to the Chairman.

An additional three Board meetings were held to consider specific matters for the separation of the Gas Distribution business. All directors were given sufficient notice to attend these meetings. The rigour and preparation for these additional Board meetings followed the Board's embedded governance practices, and, as previously reported, were supported by a programme of technical, financial, legal and regulatory briefings.

Board remuneration

The Directors of the Company are not separately remunerated in that capacity with the exception of the SIDs. The remuneration of any Director, who is also a member of the Board of National Grid, is determined by the Remuneration Committee of the Board of National Grid, as set out in its annual report and accounts. The remuneration of other Directors is determined in accordance with National Grid's remuneration policies for employees. As required by Section 33f of the Gas Act 1986, the Company has provided to Ofgem details of the linkages between Directors' remuneration and service standards.

During the year, as part of the Company wide compensation review, the Board reviewed and approved an increase in the non-executive fee paid to the SIDs. The increase in fee reflected the increased ongoing requirements of the Board, their individual appointments as Chairmen of the Audit Committee and Business Separation Compliance Committee and considered a benchmarking review of fees paid to external independent directors. Due to the lack of comparator information available for the specific role of a SID, the roles of senior independent directors were used in the benchmarking exercise.

Committees

The Board has established a number of committees and sub-committees which assist it in its activities and operate within agreed Terms of Reference and a framework of Delegations of Authority. The Committees of the Board are listed below:

- Gas Transmission Executive Committee
- System Operator Executive Committee
- Business Separation Compliance Committee
- Finance Committee
- Pension Committee
- Audit Committee

The Company does not have a Nominations or Remuneration Committee as these functions are provided by National Grid plc. See the Annual Report and Accounts of National Grid plc for further information about these committees.

Prior to the separation of the Gas Distribution business, the Board had an established Distribution Executive Committee which functioned specifically to assist the Board with the activities of the Gas Distribution business.

The separation of the Gas Distribution business had a number of effects on the work of certain Board's committees.
Prior to the separation of the Gas Distribution business, specific matters required consideration to prepare the Gas Distribution business for separation and sale. These matters were considered by the appropriate committees in line with their Terms of Reference and further details are provided below.

Following separation of the Gas Distribution business, certain activities were transferred to the governance framework of NGGD. The work of the Distribution Executive Committee and the Distribution Business Separation Compliance Committee was transferred in its entirety. The Finance Committee's activities in relation to the Gas Distribution business were transferred to the governance framework of NGGD.

Gas Transmission Executive Committee

The purpose of the Gas Transmission Executive Committee (GTEC) is to direct the affairs of the Gas Transmission Owner business on behalf of its Board and to perform an assurance role within the context of the overall RIIO networks governance framework and oversee the performance of any sub-committees reporting to it. The Committee's remit extends to approving the Gas Transmission strategies and business objectives for managing the RIIO contract and for approving opportunities to deliver value within that contract in accordance with published Delegation of Authority (DoA) limits.

Additionally the Committee performs assurance responsibilities for the Gas Transmission Owner business performance frameworks including the monitoring of performance against the RIIO contract, financial targets, high-level risks and audit outcomes. To this end the Committee receives summary reports from Process Performance Meetings, Regulatory Commercial Committees and Business Partner Functions.

GTEC acts within National Grid's overall corporate governance framework and delegated authorities and is responsible for the operational and financial management of the Gas Transmission Owner business. Membership of this Committee comprises at least two Directors of the Company, senior managers of the Gas Transmission Owner business and certain other senior managers. Attendance of the voting members is expressed as the number of meetings attended out of the number eligible to attend, and includes attendance by a nominated deputy during the year to 31 March 2017. There were twelve Committee meetings held during the year.

		Attendance
Pauline Walsh	Director, Gas Transmission Owner	12 of 12
Isabelle Haigh	Head of Business Improvement	11 of 12
Darren Elsom [1]	Head of Network Engineering	1 of 1
David Salisbury [2]	Head of Network Engineering	10 of 11
Ian Radley	Head of Gas Construction	12 of 12
Andy Malins	Head of Network Capability & Operations, Gas	12 of 12
Alan Rankin [3]	Group Head of Process Safety & UK Safety	1 of 1
Bob Watson [4]	Group Head of Process Safety & UK Safety	4 of 9
Mark Ripley [5]	Director, UK Regulation	3 of 3
Chris Bennett [6]	Director, UK Regulation	6 of 9
Vicki Flindall	Lead Finance Business Partner. GTO	12 of 12

1. Resigned April 2016
2. Appointed May 2016
3. Resigned April 2016
4. Appointed July 2016
5. Resigned June 2016
6. Appointed June 2016

During a period of changing senior management in the safety function, safety was represented at a sub-committee of GTEC, being the Gas Transmission Safety Health and Environment (GTSHE) committee, and any matters of concern from GTSHE were escalated as appropriate.

The GTEC has a number of sub-committees dealing with matters such as investment governance and coordination of operations.

Distribution Executive Committee

Up until the legal separation of the Gas Distribution business on the 1 October, the Distribution Executive Committee (DEC) acted within National Grid's overall corporate governance framework and delegated authorities and was responsible for directing the affairs and taking all substantial decisions , including the operational and financial management of the Gas Distribution business. Membership of DEC comprised two Directors of the Company and senior managers of the Gas Distribution business. Attendance of the voting members is set out and below and is expressed as the number of meetings attended out of the number eligible to attend, and includes attendance by a nominated deputy from April 2016 to September 2016. There were three Committee meetings held during this period.

		Attendance
Chris Train (Chair)	Director Gas Distribution	3 of 3
Carla James	HR Business Partner	3 of 3
Julian Allsopp	Lead Finance Business Partner, Gas Distribution	2 of 3
Hilary Buxton	Replace & Extend Process Manager and Head of Emergency Response & Repair Process (ER&R)	3 of 3
Ed Syson	Director of Operations	3 of 3
David Parkin	Director of Network Strategy	3 of 3
Ann Marie Ward	Head of Customer Operations	1 of 3
Jonathan Callighan	Head of Gas Distribution Strategic Partnerships	3 of 3
Leigh Page	Seconded Head of Stakeholder Delivery	1 of 1

The DEC had a number of sub-committees dealing with matters such as investment, governance and coordination of operations.

System Operator Executive Committee

The System Operator Executive Committee (SOEC) acts within National Grid's overall corporate governance framework and delegated authorities and is responsible for the strategic direction of Great Britain SO activities (Gas and Electricity combined) and RIIO incentive and output performance measures. The SOEC was set up following the implementation of the new UK Operating Model in 2013. Membership of this Committee comprises Directors of the Company, senior managers of the Transmission business and certain other senior managers. Attendance of the voting members is set out below and is expressed as the number of meetings attended out of the number eligible to attend, and includes attendance by a nominated deputy during the year to 31 March 2017. There were five Committee meetings held during the year.

		Attendance
Cordi O'Hara	Director, UK System Operator	4 of 5
Phil Shepard	Director, System Operations	3 of 5
Simon Johnston	Head of Business Change	5 of 5
Darren Pettifer	SO Business Partner, Finance	5 of 5
Mark Ripley [1]	Director, UK Regulation	2 of 2
Chris Bennett [2]	Director, UK Regulation	3 of 3

1. Resigned June 2016
2. Appointed June 2016

The SOEC has a number of sub-committees dealing with matters such as SO specific investments, SO Risk and Compliance and SO Incentive Performance.

Business Separation Compliance Committees

The Business Separation Compliance Committee of the Board is responsible for overseeing the duties and tasks of the Business Separation Compliance Officer and for overseeing compliance with the business separation licence conditions.

Membership of the Committee is by appointment of the Board and comprises all directors of the licensee. The Committee is chaired by Dr Catherine Bell, SID, providing independent leadership of the Committee. The Business Separation Compliance Officer/ Compliance Officer are in attendance and present reports on their duties, activities and compliance with the licence obligations.

Two Committee meetings were held during the year, with additional meetings taking place between the Chairman of the Committee and the Business Separation Compliance Officer/Compliance Officer. Following the meetings, the Chairman provided updates to the Board on matters considered at the meetings.

The separation of the Gas Distribution business required consideration and implementation of a number of matters. Prior to the separation, both the Distribution and Transmission Business Separation Compliance Committees discussed the licence changes which would be made in respect of business separation. The Business Separation Compliance Officer prepared a report on business separation compliance to provide assurance to the Board that risks had been properly mitigated prior to the completion of the sale of NGGD on 31 March 2017.

Following separation, a separate Business Separation Compliance Officer/Compliance Officer was appointed to NGGD and a new Distribution Business Separation Compliance

Committee of the NGGD Board was established. Please refer to the separate sections on Business separation and the Company's Compliance statement for further information.

Finance Committee

The Finance Committee of the Board is responsible for setting policy and grants authority for financing decisions, credit exposure, hedging and foreign exchange transactions, guarantees and indemnities subject to the risk appetite of the Board. It also approves, other treasury, tax, pension funding and insurance strategies, and if appropriate, recommends them to the Board.

Membership of the Committee comprises the Finance Director of National Grid plc and the Group Tax and Treasury Director, a director of the Board. The Committee interfaces with the Finance Committee of National Grid plc and the Board and receives reports from the Pensions Committee.

Each Board meeting considers a separate agenda item on the work of the Finance Committee. Financial reporting on the financing activities, taxation and financial costs and liabilities of the pension schemes is provided through the regular financial management reports discussed at each board meeting.

As part of the separation of the Gas Distribution business, the Finance Committee considered matters in relation to the debt restructuring exercise and issue of new debt, and received updates on tax, insurance and pensions matters required to prepare the Gas Distribution business for sale.

Following separation of the Gas Distribution business, the activities specifically related to the Gas Distribution business were transferred to the governance framework of NGGD. Share capital remains unchanged. See note 21 to the consolidated financial statement for further details.

Pension committee

The Board's governance of the Company's pension schemes is provided through a Pensions Committee, which sits together with the Group Retirement Plans Committee under similar Terms of Reference.

Membership of the Committee comprises the Finance Director of National Grid plc and at least three global representatives including the Group Tax and Treasury Director, Global HR Director and Global Head of Pensions of National Grid plc. The Committee reports at least annually to the Finance Committee and provides an update to the Board through the Group Tax and Treasury Director.

Focus and oversight on pension matters is provided through the Board considering pensions as a separate agenda item at each of its board meetings.
In preparation for the separation and disposal of a majority stake in the Gas Distribution business, the Board considered the activities required in relation to pensions, considering the wide range of stakeholders who would have an interest in this matter. The National Grid UK Pension Scheme ("NGUK Pension Scheme") is a defined benefit post-retirement scheme and has members from National Grid's Gas Transmission, Gas Distribution, Metering businesses and other National Grid corporate entities in the UK.

To prepare for the disposal of a majority stake in the Gas Distribution business it was necessary to sectionalise the NGUK Pension Scheme into three legally ring-fenced funds within the same scheme (Gas Distribution, Gas Transmission and Non-Regulated), a matter which required approval by the Board. The Board sought and received assurance and information on the governance processes for the sectionalisation process and engagement processes with the Pensions Trustees, Pension Regulator and OFGEM. The Board were supported by members of the National Grid project team managing the sale of the Gas Distribution business, Group pensions function and the Pensions Committee, through regular Board meeting updates and technical briefings. The Board were apprised of the financial impact of the sectionalisation of the NGUK Pension Scheme through reports from the Finance function.

Looking to the future management and operation of the gas distribution fund within the NGUK Pension Scheme, the Board considered and discussed the Board's, and wider National Grid group's, responsibilities to the range of stakeholders. The Board considered the governance processes and legal agreements that would be put in place to manage and mitigate risks both following separation of the Gas Distribution business into a legally separate company and once National Grid became a minority shareholder following disposal of the majority stake in this company.

Audit Committee

The Audit Committee's role is to keep under review the Company's financial reporting and internal controls and their effectiveness, together with reviewing the Company's risk management processes. It also reviews the external audit plan and reviews the external auditors' findings.

Since its conception in November 2014, the Audit Committee's role has developed and enhanced, providing the assurance required by the Board on matters within its authority. The Chairman provides a report on the meeting to the following Board meeting, and where applicable makes recommendations to the Board. The Board considers these recommendations and, where required, seeks further assurance and details to be brought to the Board.
To strengthen the governance links to National Grid, the SIDs hold an annual meeting with the Chairman of the National Grid plc Audit Committee.

The preparation and management of the Audit Committee's annual meeting schedule follows the same governance processes as those for the Board. Technical briefings and meetings with the UK Chief Financial Officer and members of the financial function are held before meetings, as required, to provide further details on matters to be discussed during the meetings.

Five scheduled meetings took place during the last financial year. Committee membership and attendance at meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2017.

		Attendance
Clive Elphick (Chair)	Sufficiently Independent Directors	5 of 5
Catherine Bell	Sufficiently Independent Directors	5 of 5
Andy Agg	Group Tax and Treasury Director	4 of 5

An additional Audit Committee meeting was held to consider specific matters for the separation of the Gas Distribution business. The rigour and preparation for this additional Audit Committee meeting followed the Board's embedded governance practices, and, as previously reported, was supported by a programme of briefings.

Areas of focus

The Audit Committee meetings considered a programme of matters comprising those which were aligned to that of the National Grid plc Audit Committee and specific matters as they related to the Company, as a listed and regulated entity and as defined in the Terms of Reference for the Committee. Examples of key areas of focus included:

Sale of the Gas Distribution business

Statutory and regulatory accounting statements
Interim financial statements

- Going concern statements
- Fair, balanced and understandable statements
- Financial reporting
- Internal controls and processes
- Regulatory to RIIO accounts transition
- Risk management processes
- Compliance matters, including compliance with licence obligations
- Internal (corporate) audit plan

Significant issues

The most significant issue the Committee considered during the year was the impact of the separation and sale of the Gas Distribution business on the Company's interim and year end financial statements. This included consideration of the issues around separating the Gas Distribution operations from the retained business; the judgements made by management when considering what items should be included in the exceptional gain on disposal; the financing of the new Gas Distribution business and impact on NGG; and the basis of preparation of the carve out accounts. The Committee also had specific deep dive sessions with the finance and regulatory teams as well as discussion and challenge at each Committee meeting during the year.

The Committee considered the impact of the separation of the Gas Distribution business on the risk management and internal controls frameworks. This risk was reviewed throughout the process, reviewing the progress of separation logistics and maintaining focus on the progress of critical processes, internal controls and resourcing. The Committee sought input from management, internal audit and the external auditors on the risks and mitigating actions associated with the separation process.

The Committee also received regular updates on management's response to the expected change in regulatory accounting reporting required for the implementation of RIIO accounts. Looking forwards, the Committee will continue to focus on the changes required in regulatory accounting reporting.

Looking forwards, the Committee will continue to focus on the effectiveness of the risk management and internal control processes, providing input to the Group wide processes. The Committee continues to focus on any specific risks related to non-compliance with licence obligations and requests senior managers and external advisers to attend meetings to provide more detailed presentations on matters of non-compliance. The Committee informs the Board of risks and mitigating actions in relation to licence breaches that has been brought to the Committee's attention, enabling the Board to discuss and determine further action as required. Further detail on the risk management and internal control processes can be found in the internal control and risk management section, see page 18.

External audit

The Committee is responsible for overseeing relations with the external auditors, as part of the Group wide external audit arrangements. Each Committee meeting is preceded by a meeting between the SIDs and the external auditors, without management present, to allow independent discussions on any matters the auditors would like to bring to the attention of the Committee.

The Committee reviews the audit plan and audit findings in respect of the audit of the statutory and regulatory accounts. The Committee also engages on auditor recommendations for improvements around internal controls. Through regular management reporting on internal controls, the Committee is able to monitor progress of the actions being taken.

Following the National Grid plc Audit Committee audit tender process, Deloitte LLP will be recommended for appointment at the National Grid plc 2017 AGM, with the appointment effective for the year ending 31 March 2018. In preparation for the change in external auditor, the Audit Committee has received reports and updates on the transition process from management and the external auditors.

Internal (corporate) audit
The Company does not have a separate internal audit function. This function is provided by National Grid's Corporate Audit function. The National Grid Corporate Audit function provides independent, objective, assurance to the National Grid Electricity Transmission Audit Committee, Safety, Environment and Health Committee (SEH) and Executive Committees on whether our existing control and governance frameworks are operating effectively in order to meet National Grid's strategic objectives. Assurance work is conducted and managed in accordance with the IIA international standards for the Professional Practice of Internal Auditing and Code of Ethics.

Audit work is delivered by a combination of suitably qualified employee, who typically have either a finance or operational business background and external co-source partners, where specific specialist skills are required.

Inputs to the audit plan include principal risks, risk registers, corporate priorities, and external research of emerging risks and trends, and discussions with senior management to make sure the plan aligns with the Committee and Company's view of risk. The audit plan is considered and approved by the Committee annually and progress against the plan is monitored throughout the year.

The Committee received regular controls updates from the Corporate Audit team. Management actions on audit findings have continued to be a focus at Executive meetings resulting in greater visibility of audit findings, increased ownership of actions and greater engagement by senior management.

Auditors' independence and objectivity
As highlighted in National Grid's Annual Report and Accounts for 2016/17 the independence of the external auditors is essential to the provision of an objective opinion on the true and fair view presented in the financial statements.

Consistent with prior years, an annual review was conducted by the Audit Committee of the level and make-up of the external audit and non-audit fees and the effectiveness, independence and objectivity of PwC. Following this process, the Audit Committee was satisfied with the effectiveness, independence and objectivity of PwC and recommended to the Board their reappointment for the year ended 31 March 2017 at the 2016 AGM.

Following the audit tender, the Audit Committee has recommended to the Board the appointment of Deloitte as auditors for the year ending 31 March 2018. A resolution to appoint Deloitte and giving authority to the Directors to determine their remuneration will be submitted to shareholders at the 2017 AGM.

Business separation

Special Condition 4F of our Retained Distribution Networks Licence requires that the gas Distribution Network businesses comply with the Compliance Statement prepared in accordance with Special Condition 10B of our National Transmission System (NTS) gas transporter licence, which requires that the Company maintains managerial and operational systems such that:

- the Distribution Network (DN) businesses do not gain unfair commercial advantage by reason of the way the Company conducts its NTS business, as required by Standard Special Condition A6; and
- cross-subsidy between the NTS business and the DN businesses is avoided, as required by Standard Special Condition A35.

Our policy on business separation is set out in the Company's Compliance Statement.

We have taken the following specific actions to comply with the requirements of Special Condition 10B:

- established separate management committees for the gas transmission and gas distribution businesses, as described above;
- appointed separate Compliance Committees for each of the gas transmission business and the gas distribution business, as described above. Each Compliance Committee reports directly to the Board of National Grid Gas and also to the Audit Committee of National Grid; and
- appointed a Business Separation Compliance Officer, who reports to the Compliance Committees and twice yearly to the Audit Committee of National Grid.

Standard Special Condition A33 of our gas distribution transporter licence requires that the Company maintains managerial and operational systems such that:

- it's affiliate metering business does not have access to confidential information unless it is made available on an equal basis in accordance with the provisions of Standard Special Condition A33; and
- it manages and operates the transportation business in a way calculated to ensure it does not restrict, prevent or distort competition.

Our policy on business separation is set out in the Company's Compliance Statement.

We have taken the following specific actions to comply with the requirements of Standard Special Condition A33:

- established separate management for the gas distribution business and metering businesses; and
- appointed a Compliance Officer, who reports to the Directors of the licensee through the established Compliance Committee.

Directors' Report

The Directors present their report and the audited consolidated financial statements of the Group for the year ended 31 March 2017. In accordance with the requirements of the Companies Act 2006, the following sections describe the matters that are required for inclusion in the Directors' Report and were approved by the Board. Further details of matters required to be included in the Directors' Report are incorporated by reference into this report, as detailed below.

Directors

The Directors of the company who were in office during the year and up to the date of signing the financial statements were:

Andy Agg	
Julian Allsopp	Resigned 1 October 2016
Catherine Bell (SID)*	
Chris Bennett	Appointed 25 June 2016
Clive Elphick (SID)*	
Alan Foster	
Chris Murray	Resigned 27 July 2016
Cordi O'Hara	
Mark Ripley	Resigned 24 June 2016
Nicola Shaw CBE	Appointed 27 July 2016
Chris Train	Resigned 1 October 2016
Pauline Walsh	

**sufficiently independent director*

The Company has arranged, in accordance with the Companies Act 2006 and the Articles, qualifying third party indemnities against financial exposure that Directors may incur in the course of their professional duties. Equivalent qualifying third party indemnities were, and remain, in force for the benefit of those Directors who stood down from the Board during the year ended 31 March 2017. Alongside these indemnities, the Company places Directors' and Officers' liability insurance cover for each Director.

Principal activities and business review

A full description of the Company's principal activities, businesses, key performance indicators and principal risks and uncertainties is contained in the Strategic Report on pages 13 to 23, which are incorporated by reference into this report.

Material interests in shares

National Grid Gas plc is a wholly owned subsidiary undertaking of National Grid Gas Holdings Limited. The ultimate parent company of National Grid Gas plc is National Grid plc.

Dividends

During the year, interim dividends totalling £8,100 million were paid (2015/16: £620 million interim dividend). The Directors have not proposed a final dividend.

Share capital

Share capital remains unchanged. See note 21 to the consolidated financial statement for further details.

Research and development

Expenditure on research and development was £4 million during the year (2015/16: £6 million).

Financial instruments

Details on the use of financial instruments and financial risk management are included in note 25 to the consolidated financial statements.

Future developments

Details of future developments are contained in the Strategic Report.

Employee involvement

Details of how the Company involves its employees are contained in the Strategic Report on pages 16 and 17, which are incorporated by reference into this report.

Audit information

Having made the requisite enquiries, so far as the Directors in office at the date of the signing of this report are aware, there is no relevant audit information of which the auditors are unaware and each Director has taken all reasonable steps to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

Annual General Meeting

Notice of the National Grid Gas's Annual General Meeting for 2017 will be issued separately to the shareholder.

Going concern

Having made enquiries and reviewed management's assessment of the going concern assumption, the Directors consider it appropriate to prepare the financial statements on a going concern basis. The going concern basis presumes that the Company has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements are signed. More detail on our financial risks, including liquidity and solvency, is provided in note 25 to the consolidated financial statements. There have been no major changes to the Group's significant liquidity and solvency risks in the year. Although not assessed over the same period, the viability of the Group has been assessed on page 23.

On behalf of the Board

Alan Foster
Director
30 June 2017
National Grid Gas plc,
1-3 Strand, London WC2N 5EH
Registered in England and Wales Number 2006000

Introduction to the financial statements

Throughout these financial statements we have provided explanations of the disclosures and why they are important to the understanding of our financial performance and position.

Notes

Notes to the financial statements provide additional information required by statute, accounting standards or other regulations to assist in a more detailed understanding of the primary financial statements. In many notes we have included an accounting policy that describes how the transactions or balance in that note have been measured, recognised and disclosed. The basis of preparation section provides details of accounting policies that apply to transactions and balances in general.

Statement of Directors' responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland", and applicable law). In preparing the group financial statements, the directors have also elected to comply with IFRSs, issued by the International Accounting Standards Board (IASB). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and company and of the profit or loss of the group and company for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union and IFRSs issued by IASB have been followed for the group financial statements and United Kingdom Accounting Standards, comprising FRS 102, have been followed for the company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the group and company's transactions and disclose with reasonable accuracy at any time the financial position of the group and company and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

The directors are also responsible for safeguarding the assets of the group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

In the case of each director in office at the date the Directors' Report is approved:

- so far as the director is aware, there is no relevant audit information of which the group and company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the group and company's auditors are aware of that information.

Directors' Report

The Directors' Report, prepared in accordance with the requirements of the Companies Act 2006 and Disclosure Rules and Transparency Rules, on page 38, was approved by the Board and signed on its behalf.

On behalf of the Board

Alan Foster
Director
30 June 2017

Independent Auditors’ report

to the Members of National Grid Gas plc

Report on the financial statements

Our opinion

In our opinion:

- National Grid Gas plc’s group financial statements and company financial statements (the “financial statements”) give a true and fair view of the state of the group’s and of the company’s affairs as at 31 March 2017 and of the group’s profit and cash flows for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (“IFRSs”) as adopted by the European Union;
- the company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in the Basis of preparation to the financial statements, the group, in addition to applying IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).
In our opinion, the group financial statements comply with IFRSs as issued by the IASB.

What we have audited

The financial statements, included within the Annual Report and Accounts (the “Annual Report”), comprise:

- the consolidated statement of financial position as at 31 March 2017;
- the company balance sheet as at 31 March 2017;
- the consolidated income statement and consolidated statement of comprehensive income for the year then ended;
- the consolidated cash flow statement for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the company statement of changes in equity for the year then ended;
- the accounting policies; and
- the notes to the financial statements, which include other explanatory information.

The financial reporting framework that has been applied in the preparation of the group financial statements is IFRSs as adopted by the European Union, and applicable law. The financial reporting framework that has been applied in the preparation of the company financial statements is United Kingdom Accounting Standards, comprising FRS 102 “The Financial Reporting Standard applicable in the UK and Republic of Ireland”, and applicable law (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors’ Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors’ Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the group, the company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors’ Report. We have nothing to report in this respect.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Corporate Governance Statement set out on pages 29 to 36 with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements and has been prepared in accordance with applicable legal requirements; and
- the information given in the Corporate Governance Statement set out on pages 29 to 36 with respect to the company’s corporate governance code and practices and about its administrative, management and supervisory bodies complies with rules 7.2.2, 7.2.3 and 7.2.7 in the Disclosure Guidance and Transparency Rules sourcebook of the Financial Conduct Authority.

In addition, in light of the knowledge and understanding of the group, the company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the information referred to above in the Corporate Governance Statement. We have nothing to report in this respect.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Corporate governance statement

Under the Companies Act 2006 we are required to report to you if, in our opinion, a corporate governance statement has not been prepared by the company. We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of the Directors' Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the group's and the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.

Richard French (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
30 June 2017

Basis of preparation

(for National Grid Gas plc)

Accounting policies describe our approach to recognising and measuring transactions and balances in the year. Accounting policies applicable across the financial statements are shown below. Accounting policies that are specific to a component of the financial statements have been incorporated into the relevant note.

This section also shows areas of judgement and key sources of estimation uncertainty in these financial statements. In addition, we summarise new EU endorsed accounting standards, amendments and interpretations and whether these are effective in 2018 or later years, explaining how significant changes are expected to affect our reported results.

National Grid Gas plc's principal activities involve the transmission and distribution of gas in Great Britain. The Company is a public limited company incorporated and domiciled in England, with its registered office at 1-3 Strand, London WC2N 5EH.

These consolidated financial statements were approved for issue by the Board of Directors on 30 June 2017.

These consolidated financial statements have been prepared in accordance with International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and related interpretations as issued by the International Accounting Standards Board (IASB) and IFRS as adopted by the EU. They are prepared on the basis of all IFRS accounting standards and interpretations that are mandatory for periods ending 31 March 2017 and in accordance with the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the EU IAS Regulation. The comparative financial information has also been prepared on this basis.

The consolidated financial statements have been prepared on a historical cost basis, except for the recording of pension assets and liabilities, the revaluation of derivative financial instruments and investments classified as available-for-sale. These consolidated financial statements are presented in pounds sterling, which is also the functional currency of the Company.

The financial information relating to prior years has been re-presented as a result of the disposal of the UK Gas Distribution business, as described in C below. The notes to the financial statements have been prepared on a continuing basis unless otherwise stated.

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period (see accounting policy E).

A. Going concern

The Directors considered it appropriate to prepare the financial statements on a going concern basis. The going concern basis presumes that the Group has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements are signed.

B. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries. A subsidiary is defined as an entity controlled by the Company. Control is achieved where the Company has the power to affect the returns of an entity to which it is exposed or to which it has rights.

Where necessary, adjustments are made to bring the accounting policies used in the individual financial statements of the Company and its subsidiaries into line with those used by the Company in its consolidated financial statements under IFRS. Inter-company transactions are eliminated.

The results of subsidiaries (other than relating to Gas Distribution as described in C below), and associates acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition, or up to the effective date of disposal, as appropriate.

C. Disposal of UK Gas Distribution

As described further in note 7, the disposal of the Gas Distribution business completed on 1 October 2016 and as a result all assets and liabilities of UK Gas Distribution were disposed.

As Gas Distribution represents a separate major line of business, the business is classified as a discontinued operation in the consolidated income statement. This has resulted in the re-presentation of comparative financial information in the consolidated income statement and the consolidated statement of comprehensive income, split between continuing and discontinued operations.

D. Foreign currencies

Transactions in currencies other than the functional currency of the Company or subsidiary concerned are recorded at the rates of exchange prevailing on the dates of the transactions. At each reporting date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at closing exchange rates. Non-monetary assets are not retranslated unless they are carried at fair value.

Gains and losses arising on the retranslation of monetary assets and liabilities are included in the income statement, except where the adoption of hedge accounting requires inclusion in other comprehensive income see note 11.

E. Areas of judgement and key sources of estimation uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates. Information about such judgements and estimations is contained in the notes to the financial statements, and the key areas are summarised below.

Areas of judgement that have the most significant effect on the amounts recognised in the financial statements are as follows:

- Concerning the sale of UK Gas Distribution – note 7:
  - the allocation of financing costs between the continuing Group and discontinued operations; and
  - the identification and classification of costs associated with the disposal.
- the categorisation of certain items as exceptional items, and the definition of adjusted earnings – note 3.
- environmental and decommissioning provisions – note 20.

IFRS provides certain options available within accounting standards. Choices we have made, and continue to make, include the following:

- **Presentational formats:** we use the nature of expense method for our income statement and aggregate our statement of financial position to net assets and total equity. In the income statement, we present subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items and remeasurements. Exceptional items and remeasurements are presented separately on the face of the income statement.
- **Customer contributions:** contributions received prior to 1 July 2009 towards capital expenditure are recorded as deferred income and amortised in line with the depreciation on the associated asset.
- **Financial instruments:** we normally opt to apply hedge accounting in most circumstances where this is permitted.

Key sources of estimation uncertainty that have significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are as follows:

- review of residual lives, carrying values and impairment charges for other intangible assets and property, plant and equipment – notes 8 and 9.
- estimation of asset/liabilities for pensions and other post-retirement benefits – note 19.
- valuation of financial instruments and derivatives – notes 11 and 25.
- revenue recognition and assessment of unbilled revenue – note 1.
- environmental and decommissioning provisions – note 20.

In order to illustrate the impact that changes in assumptions could have on our results and financial position, we have included sensitivity analysis in note 26.

Recent accounting developments

New IFRS accounting standards and interpretations adopted in 2016/17

The Group has adopted the following amendments to standards:

- Annual improvements to IFRSs 2012-2014 Cycle;
- Amendments to IFRS 11 'Joint Arrangements';
- Amendments to IAS 1 'Presentation of Financial Statements';
- Amendments to IAS 16 'Property, Plant and Equipment'; and
- Amendments to IAS 38 'Intangible Assets'.

The adoption of these amendments has had no material impact on the results or financial statement disclosures.

New IFRS accounting standards and interpretations not yet adopted

The Company enters into a significant number of transactions that fall within the scope of IFRS 9 'Financial Instruments'(IFRS 9), IFRS 15 'Revenue from Contracts with Customers' (IFRS 15) and IFRS 16 'Leases'(IFRS 16). We are assessing the likely impact of these standards on the Group's financial statements.

i) IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 is effective for National Grid Gas in the year ending 31 March 2019.

The new standard provides enhanced detail and a five step revenue recognition approach to reflect the transfer of goods and services to customers.

The core principle of IFRS 15 is that an entity recognises revenue related to the transfer of promised goods or services when control of the goods or services passes to customers. The amount of revenue recognised should reflect the consideration to which the entity expects to be entitled in exchange for those goods or services.

This differs from the principle under the current revenue standard that requires an assessment of when risks and rewards of goods and services are transferred rather than control of those goods or services.

Detailed reviews of revenue arrangements are under way and will continue into 2017/18 as we finalise our assessment of the impact of the new standard. Based on work to date we have identified two key areas that require further analysis to determine the impact on the Company:

- the timing of recognition of customer contributions for connections. In our gas business in the UK, we recognise customer contributions when the connection is completed (the licence conditions do not require connections to be maintained over the life of the connection and therefore do not have deferred revenue for connections). IFRS 15 requires revenue to be recognised as control over the distinct and separable service is transferred to our customers. We are assessing whether this has an impact on the timing of our revenue recognition; and
- the timing of recognition of revenue in our metering business.

We plan to apply IFRS 15 using the modified retrospective approach, whereby comparatives will not be restated on adoption of the new standard but instead a cumulative adjustment will be reflected in retained earnings.

ii) IFRS 16 'Leases'

IFRS 16 is effective for National Grid in the year ending 31 March 2020, subject to EU endorsement. The Group enters into a significant number of operating lease transactions as well as certain power purchase arrangements. Under IFRS 16, our operating leases will be accounted for on the balance sheet as 'right-of-use' assets. This treatment will increase both our assets and liabilities and subsequently, an increase to finance costs and depreciation and a reduction in rental costs. The outcome of our conclusions will have an impact on how we account for our operating leases and power purchase arrangements. We are also performing an assessment of our revenue and service contracts to determine whether we have the right to use assets under those contracts and whether they fall within the scope of IFRS 16. We plan to apply IFRS 16 using the modified retrospective approach, whereby comparatives will not be restated on adoption of the new standard but instead a cumulative adjustment will be reflected in retained earnings.

iii) IFRS 9 'Financial Instruments'

IFRS 9 is effective for National Grid in the year ending 31 March 2019. The changes to IFRS 9 principally impact the accounting for the classification of financial instruments, impairment of financial instruments and hedge accounting. The key change influences the future assessment of impairments using an 'expected loss' method rather than current 'incurred loss' method; this will result in impairments typically being recorded earlier.

To date we have not identified any significant changes to the accounting for financial liabilities and the impact on debt/derivatives on the balance sheet is anticipated to be limited.

We are currently evaluating the impact of the hedge accounting guidance in the new standard. It is possible that changes in requirements will allow the opportunity to apply hedge accounting in a wider range of scenarios.

iv) Other

In addition, the following new accounting standards and amendments to existing standards have been issued but are not yet effective have not yet been endorsed by the EU:

- Amendments to IAS 12 'Income Taxes';
- IAS 7 'Cash Flow Statements';
- Amendments to IFRS 2 'Share Based Payments';
- Amendments to IAS 7 'Statement of Cash Flows';
- Annual Improvements to IFRS Standards 2014-2016 Cycle;
- IFRIC 22 'Foreign Currency Transactions and Advance Consideration';
- Amendments to IAS 40 'Investment Property'.

Effective dates remain subject to the EU endorsement process.

The company is currently assessing the impact of the above standards, but they are not expected to have a material impact. The company has not early adopted any other standard, amendment or interpretation that was issued but is not yet effective.

Consolidated income statement

for the years ended 31 March

	Notes	2017 £m	2017 £m	2016 £m re-presented[1]	2016 £m re-presented[1]
Continuing operations					
Revenue	1 (a)		**1,340**		1,239
Operating costs	2		**(876)**		(666)
Operating profit					
Before exceptional items	1 (b)	**573**		573	
Exceptional items	3	**(109)**		-	
Total operating profit	1 (b)		**464**		573
Finance income	4		**5**		1
Finance costs					
Before exceptional items and remeasurements	4	**(160)**		(121)	
Exceptional items and remeasurements	3, 4	**(7)**		(9)	
Total finance costs	4		**(167)**		(130)
Profit/(loss) before tax					
Before exceptional items and remeasurements		**418**		453	
Exceptional items and remeasurements	3	**(116)**		(9)	
Total profit before tax			**302**		444
Tax					
Before exceptional items and remeasurements	5	**(66)**		(100)	
Exceptional items and remeasurements	3, 5	**63**		48	
Total tax	5		**(3)**		(52)
Profit after tax					
Before exceptional items and remeasurements		**352**		353	
Exceptional items and remeasurements	3	**(53)**		39	
Profit after tax from continuing operations		**299**		392	
Discontinued operations					
Profit after tax from discontinued operations					
Before exceptional items and remeasurements	7	**259**		602	
Exceptional items and remeasurements	7	**55**		115	
Gain on disposal of discontinued operations after tax	7	**4,237**		-	
Total profit after tax from discontinued operations		**4,551**		717	
Profit for the year			**4,850**		1,109
Attributable to:					
Equity shareholders of the parent					
From continuing operations			**299**		392
From discontinued operations			**4,548**		715
			4,847		1,107
Non-controlling interests					
From continuing operations			**-**		-
From discontinued operations			**3**		2
			3		2
			4,850		1,109

[1]Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation. Further information is provided in note 7.

Consolidated statement of comprehensive income

for the years ended 31 March

	Notes	2017 £m	2016 £m re-presented[1]
Profit for the year		**4,850**	1,109
Other comprehensive income from continuing operations:			
Items from continuing operations that will never be reclassified to profit or loss			
Remeasurement gains of pension assets		**134**	-
Tax on items that will never be reclassified to profit or loss		**(23)**	-
Total items from continuing operations that will never be reclassified to profit or loss		**111**	-
Other comprehensive income from continuing operations:			
Items from continuing operations that may be reclassified subsequently to profit or loss			
Net (losses)/gains in respect of cash flow hedges[2]		**(2)**	2
Transferred to profit or loss on cash flow hedges		**7**	10
Tax on items that may be reclassified subsequently to profit or loss	5	**(2)**	(3)
Total items from continuing operations that may be reclassified subsequently to profit or loss		**3**	9
Other comprehensive income for the year, net of tax from continuing operations		**114**	9
Other comprehensive income/(loss) for the year, net of tax from discontinued operations		**51**	(14)
Other comprehensive income/(loss) for the year, net of tax		**165**	(5)
Total comprehensive income for the year from continuing operations		**413**	401
Total comprehensive income for the year from discontinued operations		**4,602**	703
Total comprehensive income for the year		**5,015**	1,104
Total comprehensive income for the year			
Attributable to:			
Equity shareholders of the parent			
From continuing operations		**413**	401
From discontinued operations		**4,599**	701
		5,012	1,102
Non-controlling interests			
From continuing operations		**-**	-
From discontinued operations		**3**	2
		3	2
		5,015	1,104

[1]Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation. Further information is provided in note 7.

[2]The value of derivatives held to hedge cash flows is affected by changes in expected interest rates and in exchange rates. The net loss for the year was £2m (2016: gain of £2m)

Consolidated statement of changes in equity

	Share capital £m	Share premium account £m	Retained earnings £m	Cash flow hedge reserve £m	Other reserves £m	**Shareholders' equity £m**	Non-controlling interests £m	**Total equity £m**
As at 1 April 2015	45	204	4,908	(56)	1,332	**6,433**	2	**6,435**
Profit for the year	-	-	1,107	-	-	**1,107**	2	**1,109**
Total other comprehensive loss for the year	-	-	-	(5)	-	**(5)**	-	**(5)**
Total comprehensive income/(loss) for the year	-	-	1,107	(5)	-	**1,102**	2	**1,104**
Equity dividends	-	-	(620)	-	-	**(620)**	-	**(620)**
Other movements in non-controlling interests	-	-	-	-	-	**-**	(2)	**(2)**
Share-based payments	-	-	5	-	-	**5**	-	**5**
Tax on share-based payments	-	-	1	-	-	**1**	-	**1**
As at 31 March 2016	45	204	5,401	(61)	1,332	**6,921**	2	**6,923**
Profit for the year	-	-	4,847	-	-	**4,847**	3	**4,850**
Total other comprehensive income for the year	-	-	111	54	-	**165**	-	**165**
Total comprehensive income for the year	-	-	4,958	54	-	**5,012**	3	**5,015**
Equity dividends	-	-	(8,100)	-	-	**(8,100)**	-	**(8,100)**
Other movements in non-controlling interests	-	-	-	-	-	**-**	(5)	**(5)**
Share-based payments	-	-	7	-	-	**7**	-	**7**
Tax on share-based payments	-	-	(1)	-	-	**(1)**	-	**(1)**
At 31 March 2017	**45**	**204**	**2,265**	**(7)**	**1,332**	**3,839**	**-**	**3,839**

The cash flow hedge reserve will be continuously transferred to the income statement until the borrowings are repaid. The amount due to be released from reserves to the income statement next year is £5m (2016: £7m), and the remainder released with the same maturity profile as borrowings due after more than one year.

Other reserves comprise the capital redemption reserve arising from the refinancing and restructuring of the Lattice Group in 1999. It represents the amount of the reduction in the share capital of the Company as a consequence of that restructuring. As the amounts included in other reserves are not attributable to any of the other classes of equity presented, they have been disclosed as a separate classification of equity.

Consolidated statement of financial position

as at 31 March

	Notes	**2017 £m**	2016 £m
Non-current assets			
Intangible assets	8	**136**	252
Property, plant and equipment	9	**4,339**	12,654
Other non-current assets	10	**3,429**	5,627
Derivative financial assets	11	**813**	1,014
Pensions asset	19	**45**	-
Total non-current assets		**8,762**	19,547
Current assets			
Inventories and current intangible assets	12	**20**	26
Trade and other receivables	13	**520**	446
Financial and other investments	14	**1,856**	137
Derivative financial assets	11	**51**	66
Cash and cash equivalents	15	**-**	-
Total current assets		**2,447**	675
Total assets		**11,209**	20,222
Current liabilities			
Borrowings	16	**(846)**	(1,842)
Derivative financial liabilities	11	**(185)**	(39)
Trade and other payables	17	**(614)**	(819)
Current tax liabilities		**(9)**	(34)
Provisions	20	**(133)**	(55)
Total current liabilities		**(1,787)**	(2,789)
Non-current liabilities			
Borrowings	16	**(4,640)**	(7,261)
Derivative financial liabilities	11	**(234)**	(527)
Other non-current liabilities	18	**(189)**	(1,047)
Deferred tax liabilities	5	**(366)**	(1,548)
Provisions	20	**(154)**	(127)
Total non-current liabilities		**(5,583)**	(10,510)
Total liabilities		**(7,370)**	(13,299)
Net assets		**3,839**	6,923
Equity			
Share capital	21	**45**	45
Share premium account		**204**	204
Retained earnings		**2,265**	5,401
Cash flow hedge reserve		**(7)**	(61)
Other reserves		**1,332**	1,332
Shareholders' equity		**3,839**	6,921
Non-controlling interests		**-**	2
Total equity		**3,839**	6,923

These consolidated financial statements set out on pages 47 to 86 were approved by the Board of Directors and authorised for issue on 30 June 2017. They were signed on its behalf by:

Nicola Shaw Chair

Alan Foster Director

National Grid Gas plc
Registered number: 2006000

Consolidated cash flow statement

for the years ended 31 March

	Notes	2017 £m	2016 re-presented[1] £m
Cash flows from operating activities			
Total operating profit	1(b)	**464**	573
Adjustments for:			
Exceptional items	3	**109**	-
Depreciation, amortisation and impairment		**258**	259
Share-based payment charge		**4**	2
Changes in working capital		**(43)**	(115)
Changes in provisions		**(65)**	-
Loss on disposal of property, plant and equipment and intangible assets		**18**	10
Cash flows relating to exceptional items		**(22)**	-
Cash generated from operations		**723**	729
Tax paid		**(30)**	(81)
Net cash inflow from operating activities - continuing operations		**693**	648
Net cash inflow from operating activities - discontinued operations		**460**	1,089
Cash flows from investing activities			
Purchases of intangible assets		**(26)**	(42)
Purchases of property, plant and equipment		**(220)**	(182)
Disposals of property, plant and equipment		**-**	1
Repayment of loan by group undertaking		**2,183**	-
Interest received		**5**	1
Movement in short-term financial investments		**(1,719)**	246
Net cash flow used in investing activities - continuing operations		**223**	24
Net cash flow from/(used in) investing activities - discontinued operations[2]		**6,585**	(577)
Cash flows from financing activities			
Repayment of loans		**(53)**	-
Net settlement of short-term borrowings and derivatives		**80**	(403)
Interest paid		**(93)**	(97)
Dividends paid to shareholders		**(8,100)**	(620)
Net cash flow used in financing activities - continuing operations		**(8,166)**	(1,120)
Net cash flow from/(used in) financing activities - discontinued operations		**204**	(72)
Net decrease in cash and cash equivalents	22(b)	**(1)**	(8)
Net cash and cash equivalents at the start of the year		**(7)**	1
Net cash and cash equivalents at the end of the year	15	**(8)**	(7)

[1]Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation. Further information is provided in note 7.

[2] Included within net cash flow from investing activities - discontinued operations is £6,899m of cash proceeds from the sale of the Gas Distribution business.

Notes to the consolidated financial statements - analysis of items in the primary statements

1. Segmental analysis

This note sets out the financial performance for the year split into the different parts of the business (operating segments). We monitor and manage the performance of these operating segments on a day-to-day basis.

We work with our regulators to obtain robust regulatory agreements that balance the risks we face with the opportunity to deliver reasonable returns for our investors. Our regulated businesses earn revenue for the transmission and distribution (discontinued) services they have provided during the year. In any one year, the revenue recognised may differ from the revenue allowed under our regulatory agreements and any such timing differences are adjusted against future prices.

Revenue primarily represents the sales value derived from the transmission and distribution (discontinued) of gas and the provision of gas metering services during the year including an assessment of the value of services provided, but not invoiced, at the year end. It excludes value added tax and intra-group sales.

The sales value for the transmission and distribution (discontinued) of gas is largely determined from the amount of system capacity sold for the year, and the amount of gas transported for the year, evaluated at contractual prices on a monthly basis. The sales value for the provision of gas metering services is largely derived from monthly charges for the provision of individual meters under contractual arrangements.

Where revenue for the year exceeds the maximum amount permitted by regulatory agreement, and adjustments will be made to future prices to reflect this over-recovery, a liability for the over-recovery is not recognised as such an adjustment to future prices relates to the provision of future services. Similarly, an asset is not recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

Revenue includes income arising from the sale of properties as a result of property management activities, from the sale of emission allowances and from the recovery of pension deficit from other gas transporters under regulatory arrangement.

We present revenue and the results of the business analysed by operating segment, based on the information the Board of Directors uses internally for the purposes of evaluating the performance of operating segments and determining resource allocation between operating segments. The Board is National Grid Gas plc's chief operating decision-making body (as defined by IFRS 8 'Operating Segments') and assesses the performance of operations principally on the basis of operating profit before exceptional items and remeasurements (see note 3).

There has been no change to the way in which our businesses have reported internally during the year. However, for the purpose of this note, the reporting structure for the year ended 31 March 2017 has been updated to show the Gas Distribution segment as a discontinued operation together with the results of Xoserve Limited. The following table describes the main activities for each operating segment:

Gas Transmission - The gas transmission network in Great Britain and liquefied natural gas (LNG) storage activities
Gas Distribution (discontinued) - Four of the eight regional networks of Great Britain's gas distribution system

The reporting structure including comparatives for the year ended 31 March 2016 has been updated to show the previously reported Gas Distribution segment within discontinued operations.

Other activities relate to the gas metering business which provides regulated gas metering activities in the UK, together with corporate activities. Xoserve Limited (discontinued) provides transportation transaction services on behalf of all the major gas network transportation companies. The results for the year ending 31 March (including comparatives) have been included in 'discontinued operations'.

Sales between businesses are priced having regard to the regulatory and legal requirements that the businesses are subject to, which include requirements to avoid cross-subsidies.

1. Segmental analysis (continued)

(a) Revenue

	2017			2016 re-presented[1]		
	Total sales £m	**Sales between segments £m**	**Sales to third parties £m**	Total sales £m	Sales between segments £m	Sales to third parties £m
Operating segment						
Gas Transmission	**1,095**	**(41)**	**1,054**	1,047	(107)	940
Other activities	**286**	**-**	**286**	299	-	299
Continuing operations	**1,381**	**(41)**	**1,340**	1,346	(107)	1,239
Discontinued operations	943	(16)	927	1,973	(60)	1,913

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

Analysis of revenue by major customer:

No single customer contributed 10% or more to the Group's continuing revenue in either 2017 or 2016.

(b) Operating profit

A reconciliation of the operating segments' measure of profit to total profit before tax is provided below. Further details of the exceptional items and remeasurements are provided in note 3.

	Before exceptional items and remeasurements		After exceptional items and remeasurements	
	2017 £m	2016 £m re-presented[1]	**2017 £m**	2016 £m re-presented[1]
Operating segment				
Gas Transmission	**419**	400	**330**	400
Other activities	**154**	173	**134**	173
Continuing operations	**573**	573	**464**	573
Discontinued operations	**396**	873	**396**	857
Reconciliation to profit before tax from continuing operations:				
Operating profit	**573**	573	**464**	573
Finance income	**5**	1	**5**	1
Finance costs	**(160)**	(121)	**(167)**	(130)
Profit before tax from continuing operations	**418**	453	**302**	444
Profit before tax from discontinued operations	**328**	758	**319**	742

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

(c) Property, plant and equipment and intangible assets

	Net book value of property, plant and equipment and intangible assets		Capital expenditure		Depreciation and amortisation	
	2017 £m	2016 £m re-presented[1]	**2017 £m**	2016 £m re-presented[1]	**2017 £m**	2016 £m re-presented[1]
Operating segments						
Gas Transmission	**4,165**	4,140	**214**	186	**182**	178
Other activities	**310**	343	**28**	38	**76**	81
Continuing operations	**4,475**	4,483	**242**	224	**258**	259
Discontinued operations	**-**	8,423	284	567	158	303
Continuing operations by asset type						
Property, plant and equipment	**4,339**	4,364	**216**	182	**229**	238
Intangible assets	**136**	119	**26**	42	**29**	21
	4,475	4,483	**242**	224	**258**	259
Discontinued operations by asset type						
Property, plant and equipment	**-**	8,290	**284**	543	**135**	260
Intangible assets	**-**	133	**-**	24	**23**	43
	-	8,423	**284**	567	**158**	303

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

2. Operating costs

Below we have presented separately certain items included in our operating costs from continuing operations. These include a breakdown of payroll costs (including disclosure of amounts paid to key management personnel) and fees paid to our auditors.

	Before exceptional items and remeasurements		Exceptional items and remeasurements		Total	
	2017 £m	2016 £m re-presented[1]	**2017 £m**	2016 £m re-presented[1]	**2017 £m**	2016 £m re-presented[1]
Depreciation and amortisation	**258**	259	**-**	-	**258**	259
Payroll costs	**125**	130	**-**	-	**125**	130
Purchases of gas	**67**	74	**-**	-	**67**	74
Rates	**101**	100	**-**	-	**101**	100
Pension deficit charges [2]	**88**	86	**22**	-	**110**	86
Inventory consumed	**23**	13	**-**	-	**23**	13
Operating leases	**5**	5	**-**	-	**5**	5
Research and development expenditure	**4**	6	**-**	-	**4**	6
Other	**96**	(7)	**87**		**183**	(7)
Continuing operations	**767**	666	**109**	-	**876**	666

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

2 Pension deficit charges arise from recovery plan contributions to the National Grid UK Pension Scheme prior to sectionalisation of this scheme. For further details see note 19.

(a) Payroll costs

	2017 £m	2016 £m re-presented[1]
Wages and salaries	**104**	105
Social security costs	**16**	12
Pension costs (note 19)	**21**	24
Share-based payments	**4**	2
Severance costs (excluding pension costs)	**2**	6
	147	149
Less: payroll costs capitalised	**(22)**	(19)
Continuing operations	**125**	130

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

(b) Number of employees, including Directors

	31 March 2017 Number	31 March 2016 Number re-presented[1]	**Monthly average 2017 Number**	Monthly average 2016 Number re-presented[1]
Gas Transmission	**932**	895	**916**	878
Other[2]	**993**	1,219	**1,090**	1,208
Continuing operations	**1,925**	2,114	**2,006**	2,086
Discontinued operations[3]	**-**	4,014	**4,021**	3,968

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

2 Other comprises National Grid Metering and employees working in shared services supporting the Gas Transmission businesses.

3 Discontinued for 2017 represents the average number of employees employed for the six months prior to the Gas Distribution business being hived out on 1 October 2016.

(c) Key management compensation

	2017 £m	2016 £m
Short-term employee benefits	**3**	3
Post-employment benefits	**-**	1
Share-based payment	**1**	2
Continuing operations	**4**	6

Key management comprises the Board of Directors of the Company together with those Executive Directors of National Grid plc who have managerial responsibility for any of the businesses of National Grid Gas plc.

2. Operating costs (continued)

(d) Directors' emoluments

The aggregate amount of emoluments (excluding social security, pensions and share-based payment) paid to Directors of the company in respect of qualifying services for 2017 was £2,184,719 (2016: £1,846,672)

Four Directors including the highest paid Director exercised share options during 2017 (2016: four Directors including the highest paid Director).

A number of the current Directors are also Directors and employees of National Grid plc or a subsidiary undertaking of that Company and are paid by these companies.

As at 31 March 2017, retirement benefits were accruing to nine Directors under a defined benefit scheme (2016: Nine Directors under a defined benefit scheme).

The aggregate emoluments for the highest paid Director were £626,609 for 2017 (2016: £441,239) and total accrued annual pension at 31 March 2017 for the highest paid Director was nil (2016: £71,618).

(e) Auditors' remuneration

	2017 **£m**	2016 £m
Audit services		
Audit of parent company and consolidated financial statements	**0.5**	0.3
Other services		
Fees payable to the company's auditors for audit-related assurance services	**0.2**	0.2
Other non audit services	**6.9**	8.0

Fees payable to the Company's auditors for audit-related assurance services represent fees payable for services in relation to engagements which are required to be carried out by the auditors. Other non audit services primarily includes amounts incurred in respect of the disposal of a majority stake in the Gas Distribution business (vendor due diligence and separation support). These fees have been subject to approval by the Audit Committee of National Grid plc.

3. Exceptional items and remeasurements

To monitor our financial performance, we use a profit measure that excludes certain income and expenses. We call that measure 'business performance' or 'adjusted profit'. We exclude items from business performance because we believe these items are individually important to understanding our financial performance. If included, these items could distort understanding of our performance for the year and the comparability between periods. This note analyses these items, which are included in our results for the year but are excluded from business performance.

Our financial performance is analysed into two components: business performance, which excludes exceptional items and remeasurements; and exceptional items and remeasurements. Business performance is used by management to monitor financial performance as it is considered that it improves the comparability of our reported financial performance from year to year. Business performance subtotals are presented on the face of the income statement or in the notes to the financial statements.

Management utilises an exceptional items framework that has been discussed and approved by the National Grid Gas plc Audit Committee. This follows a three-step process which considers the nature of the event, the financial materiality involved and any particular facts and circumstances. In considering the nature of the event, management focuses on whether the event is within the Group's control and how frequently such an event typically occurs. In determining the facts and circumstances management considers factors such as ensuring consistent treatment between favourable and unfavourable transactions, precedent for similar items, number of periods over which costs will be spread or gains earned and the commercial context for the particular transaction.

Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, significant changes in environmental or decommissioning provisions, integration of acquired businesses, gains or losses on disposals of businesses or investments and debt redemption costs as a consequence of transactions such as significant disposals or issues of equity.

Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of derivative financial instruments to the extent that hedge accounting is not achieved or is not effective. These fair values increase or decrease because of changes in financial indices and prices over which we have no control.

3. Exceptional items and remeasurements (continued)

	2017 £m	2016 £m re-presented[1]
Included within operating profit:		
Exceptional items:		
Profit on disposal of land and buildings	**109**	-
Gas holder demolition costs	**(107)**	-
Pension sectionalisation	**(89)**	-
Pension deficit charges	**(22)**	-
	(109)	-
Included within finance costs:		
Remeasurements:		
Net losses on derivative financial instruments	**(7)**	(9)
	(7)	(9)
Total included within profit before tax	**(116)**	(9)
Included within taxation:		
Exceptional credit arising on items not included in profit before tax:		
Deferred tax credit arising on the reduction in the UK tax rate	**18**	46
Tax on exceptional items	**44**	-
Tax on remeasurements	**1**	2
	63	48
Total exceptional items and remeasurements after tax	**(53)**	39
Analysis of total exceptional items and remeasurements after tax:		
Total exceptional items after tax	**(47)**	46
Total remeasurements after tax	**(6)**	(7)
Total exceptional items and remeasurements from continuing operations	**(53)**	39

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

Further detail of operating exceptional items specific to 2017

During October 2016, following the sale of the Gas Distribution business, the company sold 78 surplus land sites to a number of fellow National Grid Group undertakings, recognising a gain on disposal of £109 million. A legal agreement was entered into with these National Grid Group companies to demolish the non-operational gas holders on these sites, creating a constructive obligation for the Company. As a result a provision of £107 million has been recognised at 31 March 2017.

With effect from 1 January 2017, sectionalisation of the National Grid UK Pension Scheme was carried out, resulting in separation of the scheme into three sections, each of which are legally and actuarially separate. Section B is included within National Grid Gas plc and the associated costs of £89m have been recognised as exceptional in 2017, see note 19 for further details.

Pension deficit charges arise from the recovery plan contributions to the National Grid UK Pension Scheme for certain employees in other activities which were incurred prior to sectionalisation of the scheme, see note 19.

Remeasurements

Net losses on derivative financial instruments comprise gains and losses arising on derivative financial instruments reported in the income statement. These exclude gains and losses for which hedge accounting has been effective, which have been recognised directly in other comprehensive income or which are offset by adjustments to the carrying value of debt.

Items included within tax

The Finance No. 2 Bill 2015 resulted in a reduction in the UK corporation tax rate from 20% to 19% for the year beginning 1 April 2017, with a further reduction from 19% to 18% for the year beginning 1 April 2020. A further reduction to 17% with effect from 1 April 2020 was enacted in the Finance Act 2016. Deferred taxes at the reporting date have been measured using these enacted tax rates and reflected in these financial statements, resulting in a deferred tax credit. This credit is presented as exceptional, reflecting its nature.

4. Finance income and costs

This note details the interest income generated by our financial assets and the interest expense incurred on financial liabilities. In reporting business performance, we adjust net financing costs to exclude any net gains or losses on derivative financial instruments included in remeasurements.

	2017 £m	2016 £m re-presented[1]
Finance income		
Interest income on financial instruments	**5**	1
Finance income	**5**	1
Finance costs		
Net interest on pension asset	**(1)**	-
Interest expense on financial liabilities held at amortised cost:		
Bank loans and overdrafts	**(21)**	(15)
Other borrowings	**(204)**	(169)
Derivatives	**64**	62
Unwinding of discount on provisions	**(1)**	(1)
Other interest	**(2)**	(2)
Less: interest capitalised[2]	**5**	4
	(160)	(121)
Remeasurements		
Net gains/(losses) on derivative financial instruments included in remeasurements[3]:		
Ineffectiveness on derivatives designated as:		
Fair value hedges[4]	**21**	20
Cash flow hedges	**(3)**	(6)
Derivatives not designated as hedges or ineligible for hedge accounting	**(25)**	(23)
Exceptional items and remeasurements included within finance costs	**(7)**	(9)
	(167)	(130)
Net finance costs from continuing operations	**(162)**	(129)

1. Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.
2. Interest on funding attributable to assets in the course of construction was capitalised during the year at a rate of 3.4% (2016: 3.2%). Capitalised interest qualifies for a current year tax deduction with tax relief claimed of £1m (2016: £1m).
3. Includes a net foreign exchange loss on financing activities of £196m (2016: £77m). These amounts are offset by foreign exchange gains and losses on derivative financial instruments measured at fair value.
4. Includes a net loss on instruments designated as fair value hedges of £11m (2016: £22m) offset by a net gain of £32m (2016: £2m) arising from the fair value adjustments to the carrying value of debt.

5. Taxation

This note gives further details of the tax charge and tax liabilities, including current and deferred tax. The current tax charge is the tax payable on this year's taxable profits. Deferred tax is an accounting adjustment to provide for tax that is expected to arise in the future due to differences in accounting and tax bases.

The tax charge for the period is recognised in the income statement, the statement of comprehensive income or directly in equity, according to the accounting treatment of the related transaction. The tax charge comprises both current and deferred tax.

Current tax assets and liabilities are measured at the amounts expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted by the reporting date.

The calculation of the Group's total tax charge involves a degree of estimation and judgement, and management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred tax is provided for using the balance sheet liability method and is recognised on temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit.

Deferred tax liabilities are generally recognised on all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences arise from the initial recognition of goodwill or from the initial recognition of other assets and liabilities in a transaction (other than a business combination) that affects neither the accounting nor taxable profit or loss.

Deferred tax liabilities are recognised on taxable temporary differences arising on investments in subsidiaries and jointly controlled entities, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based on the tax rates and tax laws that have been enacted or substantively enacted by the reporting date.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred tax asset to be recovered. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company and its subsidiaries intend to settle their current tax assets and liabilities on a net basis.

Tax charged/(credited) to the income statement - continuing operations	**2017 £m**	2016 £m re-presented[1]
Tax before exceptional items and remeasurements	**66**	100
Exceptional tax on items not included in profit before tax (note 3)	**(18)**	(46)
Tax on other exceptional items and remeasurements	**(45)**	(2)
Tax on total exceptional items and remeasurements (note 3)	**(63)**	(48)
Total tax charge from continuing operations	**3**	52

Taxation as a percentage of profit before tax	**%**	% re-presented[1]
Before exceptional items and remeasurements - continuing operations	**15.8**	22.1
After exceptional items and remeasurements - continuing operations	**1.0**	11.7

The tax charge for the year can be analysed as follows:

	£m	£m re-presented[1]
Current tax		
UK corporation tax at 20% (2016: 20%)	**106**	96
UK corporation tax adjustment in respect of prior years	**(25)**	(1)
Total current tax from continuing operations	**81**	95
Deferred tax		
UK deferred tax	**(65)**	(44)
UK deferred tax adjustment in respect of prior years	**(13)**	1
Total deferred tax from continuing operations	**(78)**	(43)
Total tax charge from continuing operations	**3**	52

Tax (credited)/charged to other comprehensive income and equity	**2017 £m**	2016 £m
Current tax		
Share-based payments	**(2)**	-
Deferred tax		
Share-based payments	**1**	-
Remeasurements of net retirement benefit obligations	**23**	-
Cash flow hedges	**2**	3
	24	3
Total tax recognised in the statement of comprehensive income from continuing operations	**25**	3
Total tax recognised in the statement of comprehensive income from discontinued operations	**11**	(2)
Total tax relating to share-based payments recognised directly in equity from continuing operations	**(1)**	-
Total tax relating to share-based payments recognised directly in equity from discontinued operations	**-**	(1)
	35	-

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

5. Taxation (continued)

The tax charge for the year after exceptional items and remeasurements is lower (2016: lower) than the standard rate of corporation tax in the UK of 20% (2016: 20%):

	Before exceptional items and remeasure-ments 2017 £m	**After exceptional items and remeasure-ments 2017 £m**	Before exceptional items and remeasure-ments 2016 £m re-presented[1]	After exceptional items and remeasure-ments 2016 £m re-presented[1]
Profit before tax				
Before exceptional items and remeasurements	**418**	**418**	453	453
Exceptional items and remeasurements	**-**	**(116)**	-	(9)
Profit before tax from continuing operations	**418**	**302**	453	444
Profit before tax from continuing operations multiplied by UK corporation tax rate of 20% (2016: 20%)	**84**	**60**	91	89
Effects of:				
Adjustments in respect of prior years	**(38)**	**(38)**	-	-
Expenses not deductible for tax purposes	**26**	**26**	3	3
Non-taxable income	**(6)**	**(27)**	(5)	(5)
Impact of share-based payments	**-**	**-**	-	-
Deferred tax impact of change in UK tax rate	**-**	**(18)**	-	(46)
Other	**-**	**-**	11	11
Total tax from continuing operations	**66**	**3**	100	52
	%	**%**	% re-presented[1]	% re-presented[1]
Effective tax rate - continuing operations	**15.8**	**1.0**	22.1	11.7

1 Comparative amounts have been re-presented to reflect the classification of the Gas Distribution business as a discontinued operation.

Factors that may affect future tax charges

The Finance Act 2016 which was enacted on 15 September 2016 reduced the main rate of UK corporation tax to 17% with effect from 1 April 2020. Deferred tax balances have been calculated at this rate. Whilst the UK remains part of the EU, the evolution of the application of EU tax competition regulations continues to create uncertainty over tax legislation and at this stage it is not possible to quantify any potential impact on the financial statements. As the Group's presence is in the UK, we do not envisage a significant impact on the Group following the UK Government's decision to invoke Article 50 to leave the EU.

Taxation included within the statement of financial position

The following are the major deferred tax assets and liabilities recognised, and the movements thereon, during the current and prior reporting periods:

Deferred tax (assets)/liabilities	Pensions £m	Accelerated tax depreciation £m	Share-based payment £m	Financial instruments £m	Other net temporary differences £m	Total £m
Deferred tax assets at 31 March 2015	-	-	(5)	(6)	(8)	(19)
Deferred tax liabilities at 31 March 2015	-	1,663	-	-	10	1,673
At 1 April 2015	-	1,663	(5)	(6)	2	1,654
(Credited)/charged to income statement	-	(106)	-	(2)	1	(107)
Credited to other comprehensive income and equity	-	-	-	1	-	1
At 31 March 2016	-	1,557	(5)	(7)	3	1,548
Deferred tax assets at 31 March 2016	-	-	(5)	(7)	(6)	(18)
Deferred tax liabilities at 31 March 2016	-	1,557	-	-	9	1,566
At 1 April 2016	-	1,557	(5)	(7)	3	1,548
Credited to income statement	(15)	(124)	-	(4)	(12)	(155)
Charged to other comprehensive income and equity	23	-	1	12	-	36
Discontinued Operations	-	(1,065)	-	-	2	(1,063)
At 31 March 2017	**8**	**368**	**(4)**	**1**	**(7)**	**366**
Deferred tax assets at 31 March 2017	-	-	(4)	-	(10)	(14)
Deferred tax liabilities at 31 March 2017	8	368	-	1	3	380
At 31 March 2017	**8**	**368**	**(4)**	**1**	**(7)**	**366**

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net. The deferred tax balances (after offset) for statement of financial position purposes consist solely of deferred tax liabilities of £366m (2016: £1,548m). At the balance sheet date there were no material current deferred tax assets or liabilities (2016: £nil).

6. Dividends

Dividends represents the return of profits to shareholders. Dividends are paid as an amount per ordinary share held. We retain part of the profits generated in the year to meet future growth plans and meet our gearing target, and pay out the remainder in accordance with our dividend policy.

Interim dividends are recognised when they become payable to the Company's shareholders. Final dividends are recognised when they are approved by shareholders.

The following table shows the dividends paid to equity shareholders:

	2017		2016	
	pence (per ordinary share)	**2017 £m**	pence (per ordinary share)	2016 £m
Ordinary dividends				
Interim dividend paid in the year	**205.38**	**8,100**	15.72	620

National Grid Gas paid two dividends during the year, Interim dividend A of £5,917m and interim dividend B of £2,183m together, the interim dividends. The interim dividends were made to ensure partial distribution of the proceeds from the Gas Distribution business.

7. Discontinued Operations

Cash flows and operations that relate to a major component of the business or geographical region that has been sold or is classified as held for sale are shown separately from continuing operations. Finance income or costs are included in discontinued operations only in respect of financial assets or liabilities classified as held for sale or derecognised on sale.

Disposal of Gas Distribution

National Grid plc made an announcement, as part of the interim results release in November 2015, that it was commencing a process for the potential sale of a majority stake in the Gas Distribution business comprising four of the eight regional networks of Great Britain's gas distribution system.

As part of the preparation for the external sale, National Grid Gas plc approved the sale of the trade and assets of the Gas Distribution business to a separate statutory entity, National Grid Gas Distribution Limited. This sale was approved by the Board on 30 September 2016 and took place on 1 October 2016. This entity was sold to a National Grid Group company and National Grid Gas plc had and has no direct or indirect ownership of National Grid Gas Distribution Limited.

On 1 October 2016, the Company transferred a majority of its 56.57% shareholding in Xoserve Limited to National Grid Gas Distribution Limited, resulting in the Company retaining a minority interest of 11%.

Accordingly, the results of the Gas Distribution business and Xoserve Limited are both presented as a discontinued operations. The segmental analysis in note 2 has also been re-presented to show these both as discontinued operations.

The presentation of the 2017 income statement is required to be split between continuing and discontinued operations and to re-present results for previous periods in a comparable manner.

Revenues, operating expenses and operating profits: Discontinued results are closely aligned to the previously disclosed Gas Distribution segment, with the results of Xoserve Limited re-allocated from within Other activities.

Interest costs: Since Gas Distribution was not independently financed prior to its sale it is necessary to allocate the National Grid Gas Group's ("Group") overall financing cost between continuing and discontinued operations. In doing so, the Group has presented the results of the continuing business on a basis consistent with how it expects to finance the Group in future periods, to aid comparability in future periods. Interest costs associated with debt and derivatives which remain in the Group as at 1 October 2016 have been attributed to the continuing group in full. Interest cost relating to instruments bought back in the period since the disposal process started, debt novated across, and debt and derivatives issued by Gas Distribution as part of the financing exercise have been included within discontinued operations. The interest costs in the comparative periods for discontinued operations only includes interest that relates to the debt bought back in 2017 and the debt novated into Gas Distribution in 2017.

Tax: Tax follows the amount of revenues, operating costs and interest allocated to discontinued operations.

7. Discontinued Operations (continued)

Income statement – Discontinued operations

for the years ended 31 March

	2017 £m	2017 £m	2016 £m	2016 £m
Revenue		**927**		1,913
Operating costs		**(531)**		(1,056)
Operating profit				
Before exceptional items and remeasurements	**396**		873	
Exceptional items and remeasurements [1]	**-**		(16)	
Total operating profit from discontinued operations		**396**		857
Finance income		**1**		-
Finance costs				
Before exceptional items and remeasurements	**(69)**		(115)	
Exceptional items and remeasurements	**(9)**		-	
Total finance costs		**(78)**		(115)
Profit before tax from discontinued operations				
Before exceptional items and remeasurements	**328**		758	
Exceptional items and remeasurements	**(9)**		(16)	
Total profit before tax from discontinued operations		**319**		742
Tax from discontinued operations				
Before exceptional items and remeasurements	**(69)**		(156)	
Exceptional items and remeasurements	**64**		131	
Total tax from discontinued operations		**(5)**		(25)
Profit after tax from discontinued operations				
Before exceptional items and remeasurements	**259**		602	
Exceptional items and remeasurements	**55**		115	
Profit after tax from discontinued operations		**314**		717
Gain on disposal of discontinued operations	**4,024**		-	
Taxation on gain on disposal of discontinued operations	**213**		-	
Gain on disposal of discontinued operations after tax		**4,237**		-
Total profit after tax from discontinued operations		**4,551**		717

1 2016 includes sale preparation costs of £16m in respect of the disposal of Gas Distribution. Current year costs have been included as part of transaction costs netted off the gain on disposal.

Statement of comprehensive income - discontinued operations

for the years ended 31 March

	2017 £m	2016 £m
Profit for the year from discontinued operations	**4,551**	717
Other comprehensive income/(loss):		
Items that may be reclassified subsequently to profit or loss		
Net losses in respect of cash flow hedges	**(50)**	(19)
Transferred to profit or loss on cash flow hedges	**113**	3
Tax on items that may be reclassified subsequently to profit or loss	**(12)**	2
Total items that may be reclassified subsequently to profit or loss	**51**	(14)
Other comprehensive income/(loss) for the year, net of tax	**51**	(14)
Total comprehensive income for the year	**4,602**	703
Attributable to:		
Equity shareholders of the parent	**4,599**	701
Non-controlling interests	**3**	2
	4,602	703

7. Discontinued Operations (continued)

Gain on disposal of discontinued operations

	£m
Assets	
Intangible assets	**92**
Property, plant and equipment	**8,431**
Other non-current assets	**37**
Inventories and current intangible assets	**7**
Trade and other receivables	**225**
Cash and cash equivelents	**3**
Total assets	**8,795**
Liabilities	
Borrowings	**(4,050)**
Derivative financial liabilities	**(4)**
Other non-current liabilities	**(886)**
Deferred tax liabilities	**(1,063)**
Provisions	**(94)**
Trade and other payables	**(250)**
Total liabilities	**(6,347)**
Net assets on disposal	**2,448**
Attributable to:	
Equity shareholders	**2,443**
Non-controlling interest	**5**
	2,448
Satisfied by:	
Net consideration[1]	**7,561**
Less:	
Financing costs [2]	**(833)**
Transaction costs [3]	**(261)**
Pre-tax gain on disposal	**4,024**
Taxation	**213**
Post-tax gain on disposal	**4,237**

1 Net consideration includes loan proceeeds of £11,682 million less the extinguishment of intercompany balances of £4,121 million. This was subsequently reduced further by a non cash transfer of debt, resulting in cash proceeds of £6,899 million received in respect to sale of the Gas Distribution business.

2 £833 million of these costs relate to the financing exercise undertaken to ensure an appropriate amount of debt was placed in Gas Distribution. This includes the costs associated with buybacks of debt from the continuing Group (£444 million), losses on loans novated at fair value from the continuing Group to Gas Distribution (£264 million) as well as losses from dedesignation of cash flow hedges (£125 million) as part of liability management restructuring.

3 Transaction costs include professional services fees for the various accounting, legal and consulting work associated with the activities to prepare and structure the hive out of Gas Distribution from the Group.

8. Intangible assets

Intangible assets relate to software, which is written down (amortised) over the period we expect to receive a benefit from the asset.

Identifiable intangible assets are recorded at cost less accumulated amortisation and any provision for impairment. Intangible assets are tested for impairment only if there is some indication that the carrying value of the assets may have been impaired.

Impairments of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash generating unit to which that asset belongs is estimated. Impairments are recognised in the income statement and are disclosed separately. Any assets which suffered impairment in a previous period are reviewed for possible reversal of the impairment at each reporting date.

Internally generated intangible assets, such as software, are recognised only if: an asset is created that can be identified; it is probable that the asset created will generate future economic benefits; and that the development cost of the asset can be measured reliably. Where no internally generated intangible asset can be recognised, development expenditure is recorded as an expense in the period in which it is incurred.

Intangible assets under development are not amortised. Other non-current intangible assets are amortised on a straight-line basis over their estimated useful economic lives. The amortisation period for software is up to eight years.

	Software £m
Cost at 1 April 2015	564
Additions	66
Cost at 31 March 2016	630
Additions	26
Reclassifications [1]	3
Disposals	(10)
Disposal of discontinued operations	(300)
Cost at 31 March 2017	349
Accumulated amortisation at 1 April 2015	(314)
Amortisation charge for the year	(64)
Accumulated amortisation at 31 March 2016	(378)
Amortisation charge for the year	(52)
Disposals	9
Disposal of discontinued operations	208
Accumulated amortisation at 31 March 2017	(213)
Net book value at 31 March 2017	**136**
Net book value at 31 March 2016	252

1 Reclassifications represents amounts transferred from property, plant and equipment, see note 9.

9. Property, plant and equipment

This note shows the physical assets controlled by us. The cost of these assets primarily represents the amount initially paid for them. A depreciation expense is charged to the income statement to reflect annual wear and tear and the reduced value of the asset over time. Depreciation is calculated by estimating the number of years we expect the asset to be used (useful economic life) and charging the cost of the asset to the income statement equally over this period.

We operate a gas transmission business and therefore have a significant physical asset base. We continue to invest in our network to maintain reliability, create new customer connections and ensure our networks are flexible and resilient. Our business plan envisages these additional investments will be funded through a mixture of cash generated from operations and the issue of new debt.

Property, plant and equipment is recorded at cost, less accumulated depreciation and any impairment losses.

Cost includes the purchase price of the asset, any payroll and finance costs incurred which are directly attributable to the construction of property, plant and equipment, as well as the cost of any associated asset retirement obligations.

Property, plant and equipment includes assets in which the Company's interest comprises legally protected statutory or contractual rights of use. Additions represent the purchase or construction of new assets, including capital expenditure for safety and environmental assets, and extensions to, enhancements to, or replacement of existing assets.

All contributions received prior to 1 July 2009 towards the cost of property, plant and equipment and contributions received post 1 July 2009 towards the altering, diverting or relocating a tangible fixed asset are included in trade and other payables as deferred income and credited on a straight-line basis to the income statement over the estimated useful economic lives of the assets to which they relate.

Contributions received post 1 July 2009 towards the cost of tangible fixed assets from customers for connections to the gas transmission and distribution networks are initially recognised as deferred income and credited to revenue once the connection has been completed. Contributions received post 1 July 2009 towards the provision of ongoing access to a supply of services are recognised initially as deferred income and revenue is subsequently recognised over the period in which the service is provided.

No depreciation is provided on freehold land or assets in the course of construction. Other items of property, plant and equipment are depreciated, on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives. In assessing estimated useful economic lives, consideration is given to any contractual arrangements and operational requirements relating to particular assets. The assessment of estimated useful economic lives and residual values of assets are performed annually. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of property, plant and equipment are, in general, as shown in the table below:

Depreciation periods	Years
Freehold and leasehold buildings	up to 50
Plant and Machinery	
- mains, services and regulating equipment	30 to 100
- meters and metering equipment	10 to 16
Motor vehicles and office equipment	up to 7

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within operating profit in the income statement.

Items within property, plant and equipment are tested for impairment if there is some indication that the carrying value of the assets may have been impaired.

Impairments of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash generating unit to which that asset belongs is estimated.

Impairments are recognised in the income statement and material impairments may be disclosed separately.

Any assets which suffered impairment in a previous period are reviewed for possible reversal of the impairment at each reporting date.

9. Property, plant and equipment (continued)

	Land and buildings £m	Plant and machinery £m	Assets in the course of construction £m	Motor vehicles and office equipment £m	Total £m
Cost at 1 April 2015	423	18,711	435	548	20,117
Additions	24	584	93	24	725
Disposals	-	(38)	-	(1)	(39)
Reclassifications [1]	-	256	(262)	6	-
Cost at 31 March 2016	447	19,513	266	577	20,803
Additions	10	319	144	27	500
Disposals	(21)	(248)	(5)	(111)	(385)
Disposal of discontinued operations	(62)	(11,612)	(75)	(286)	(12,035)
Reclassifications [1]	(11)	49	(61)	20	(3)
Cost at 31 March 2017	363	8,021	269	227	8,880
Accumulated depreciation at 1 April 2015	(181)	(7,059)	-	(437)	(7,677)
Depreciation charge for the year [2]	(40)	(411)	-	(49)	(500)
Disposals	-	27	-	1	28
Accumulated depreciation at 31 March 2016	(221)	(7,443)	-	(485)	(8,149)
Depreciation charge for the year [2]	(37)	(302)	-	(25)	(364)
Disposals	17	240	-	111	368
Accumulated depreciation on disposal of discontinued operations	27	3,375	-	202	3,604
Accumulated depreciation at 31 March 2017	(214)	(4,130)	-	(197)	(4,541)
Net book value at 31 March 2017	**149**	**3,891**	**269**	**30**	**4,339**
Net book value at 31 March 2016	226	12,070	266	92	12,654

1 Represents amounts transferred between categories during 2017 and 2016, and also to intangible assets in 2017 (see note 8).

2 Includes amounts in respect of capitalised depreciation £nil (2016: £2m).

	2017 £m	2016 £m
Information in relation to property, plant and equipment		
Capitalised interest included within cost	**229**	224
Contributions to cost of property, plant and equipment included within:		
Trade and other payables	**3**	31
Non-current liabilities	**140**	1,008

10. Other non-current assets

Other non-current assets includes assets that do not fall into any other non-current asset category (such as property, plant and equipment) and the benefit to be received from the asset is not due to be received until after 31 March 2017.

	2017 £m	2016 £m
Loans and receivables - amounts owed by parent [1]	**3,426**	5,609
Prepayments	**3**	17
Other receivables	**-**	1
	3,429	5,627

1 The amount owed by the parent is non-contractual, and its fair value is approximate to book value.

11. Derivative financial instruments

Derivatives are financial instruments that derive their value from the price of an underlying item such as interest rates, foreign exchange rates, credit spreads, equity or other indices. In accordance with the National Grid Board approved policies, derivatives are transacted to manage our exposure to fluctuations in interest rate and foreign exchange rate on borrowings and other contractual cash flows. Specifically, we use derivatives to manage these risks from our financing portfolio to optimise the overall cost of accessing the debt capital markets. These derivatives are analysed below.

Derivative financial instruments are initially recognised at fair value and subsequently remeasured at fair value at each reporting date. Changes in fair values are recorded in the period they arise, in either the income statement or other comprehensive income depending on the applicable accounting standards. Where the fair value of a derivative is positive it is carried as a derivative asset, and where negative as a derivative liability.

We calculate fair value of the financial derivatives by discounting all future cash flows using the market yield curve at the reporting date. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates. In the absence of sufficient market data, fair values would be based on the quoted market price of similar derivatives. Analysis of these derivatives and the various methods used to calculate their respective fair values is detailed below and in note 25.

For each class of derivative instrument type the fair value amounts are as follows:

	2017			2016		
	Asset £m	**Liabilities £m**	**Total £m**	Asset £m	Liabilities £m	Total £m
Interest rate swaps	**363**	**(151)**	**212**	595	(346)	249
Cross-currency interest rate swaps	**486**	**(7)**	**479**	482	(13)	469
Foreign exchange forward contracts	**8**	**(4)**	**4**	2	(1)	1
Inflation linked swaps	**7**	**(257)**	**(250)**	1	(206)	(205)
Total	**864**	**(419)**	**445**	1,080	(566)	514

The maturity profile of derivative financial instruments is as follows:

	2017			2016		
	Assets £m	**Liabilities £m**	**Total £m**	Assets £m	Liabilities £m	Total £m
In one year or less	**51**	**(185)**	**(134)**	66	(39)	27
Current	**51**	**(185)**	**(134)**	66	(39)	27
In 1 - 2 years	**69**	**(52)**	**17**	21	(11)	10
In 2 - 3 years	**76**	**(30)**	**46**	43	(63)	(20)
In 3 - 4 years	**-**	**-**	**-**	80	(63)	17
In 4 - 5 years	**412**	**(7)**	**405**	-	-	-
More than 5 years	**256**	**(145)**	**111**	870	(390)	480
Non-current	**813**	**(234)**	**579**	1,014	(527)	487
	864	**(419)**	**445**	1,080	(566)	514

For each class of derivative the notional contract amounts[1] are as follows:

	2017 £m	2016 £m
Interest rate swaps	**(3,173)**	(4,378)
Cross-currency interest rate swaps	**(728)**	(913)
Foreign exchange forward contracts	**(56)**	(46)
Inflation linked swaps	**(784)**	(762)
	(4,741)	(6,099)

[1]The notional contract amounts of derivatives indicate the gross nominal value of transactions outstanding at the balance sheet date.

11. Derivative financial instruments (continued)

Where possible, derivatives held as hedging instruments are formally designated as hedges as defined in IAS 39 'Financial Instruments: Recognition and Measurement' Derivatives may qualify as hedges for accounting purposes if they are fair value hedges, cash flow hedges or net investment hedges. Our use of derivatives may entail a derivative transaction qualifying for one or more hedge type designations under IAS 39.

Hedge accounting allows derivatives to be designated as a hedge of another non-derivative financial instrument, to mitigate the impact of potential volatility in the income statement of changes in the fair value of the derivative instruments. To qualify for hedge accounting, documentation is prepared specifying the hedging strategy, the component transactions and methodology used for effectiveness measurement. National Grid Gas uses two hedge accounting methods, which are described as follows:

Fair value hedges

Fair value hedges principally consist of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and changes in the fair value of the item in relation to the risk being hedged are offset in the income statement to the extent the fair value hedge is effective. Adjustments made to the carrying amount of the hedged item for fair value hedges will be amortised over the remaining life, in line with the hedged item.

	2017	2016
	£m	£m
Cross-currency interest rate/interest rate swaps	**537**	494

Cash flow hedges

Exposure arises from the variability in future interest and currency cash flows on assets and liabilities which bear interest at variable rates or are in a foreign currency. Interest rate and cross-currency swaps are maintained, and designated as cash flow hedges, where they qualify, to manage this exposure. Fair value changes on designated cash flow hedges are initially recognised directly in the cash flow hedge reserve, as gains or losses recognised in equity and any ineffective portion is recognised immediately in the income statement. Amounts are transferred from equity and recognised in the income statement as the income or expense is recognised on the hedged item.

Forward foreign currency contracts are used to hedge anticipated and committed future currency cash flows. Where these contracts qualify for hedge accounting they are designated as cash flow hedges. On recognition of the underlying transaction in the financial statements, the associated hedge gains and losses, deferred in equity, are transferred and included with the recognition of the underlying transaction.

When a forecast transaction is no longer expected to occur, the cumulative gain or loss previously reported in equity is transferred to the income statement. Where a non-financial asset or a non-financial liability results from a forecasted transaction or firm commitment being hedged, the amounts deferred in equity are included in the initial measurement of that non-monetary asset or liability.

	2017	2016
	£m	£m
Cross-currency interest rate/interest rate swaps	**72**	162
Foreign exchange forward contracts	**4**	1
Inflation linked swaps	**-**	(85)
Cash flow hedges	**76**	78

Derivatives not in a formal hedge relationship

Our policy is not to use derivatives for trading purposes. However, due to the complex nature of hedge accounting under IAS 39 some derivatives may not qualify for hedge accounting, or are specifically not designated as a hedge where natural offset is more appropriate. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised in remeasurements within the income statement.

	2017	2016
	£m	£m
Cross-currency interest rate/interest rate swaps	**83**	62
Inflation linked swaps	**(251)**	(120)
Derivatives not in a formal hedge relationship	**(168)**	(58)

Discontinuation of hedge accounting

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, exercised or no longer qualifies for hedge accounting. At that time, any cumulative gains or losses relating to cash flow hedges recognised in equity are initially retained in equity and subsequently recognised in the income statement in the same periods in which the previously hedged item affects profit or loss, unless the hedged item is no longer expected to occur and then the amounts would be recognised immediately. For fair value hedges, the cumulative adjustment recorded to the carrying value of the hedged item at the date hedge accounting is discontinued is amortised to the income statement using the effective interest method.

Embedded Derivatives

No adjustment is made with respect to derivative clauses embedded in financial instruments or other contracts that are defined as closely related to those instruments or contracts. Consequently these embedded derivatives are not accounted for separately from the debt instrument. Where there are embedded derivatives in host contracts not closely related, the embedded derivative is separately accounted for as a derivative financial instrument.

12. Inventories and current intangible assets

Inventories represent assets that we intend to use in order to generate revenue in future periods, either by using it to fulfil a service to a customer or to maintain our network (consumables).

Inventories are stated at the lower of weighted average cost and net realisable value.

Where applicable, cost comprises direct materials and direct labour costs as well as those overheads that have been incurred in bringing the inventories to their present location and condition.

Emission allowances, principally relating to the emissions of carbon dioxide in the UK, are recorded as intangible assets within current assets and are initially recorded at cost and subsequently at the lower of cost and net realisable value. Where emission allowances are granted by relevant authorities, cost is deemed to be equal to the fair value at the date of allocation. Receipts of such grants are treated as deferred income, which is recognised in the income statement as the related charges for emissions are recognised or on impairment of the related intangible asset. A provision is recorded in respect of the obligation to deliver emission allowances and emission charges are recognised in the income statement in the period in which emissions are made.

	2017 **£m**	2016 £m
Raw materials and consumables	**18**	24
Current intangible assets - emission allowances	**2**	2
	20	26

There is a provision for obsolescence of £5m against inventories as at 31 March 2017 (2016: £5m).

13. Trade and other receivables

Trade and other receivables are amounts which are due from our customers for services we have provided. Other receivables also include prepayments made by us, for example, property lease rentals paid in advance.

Trade, loan and other receivables are initially recognised at fair value and subsequently measured at amortised cost, less any appropriate allowances for estimated irrecoverable amounts. A provision is established for irrecoverable amounts when there is objective evidence that amounts due under the original payment terms will not be collected.

Trade receivables are non-interest bearing and generally have a 30 to 90 day term. Due to their short maturities, the fair value of trade and other receivables approximates their book value.

	2017 **£m**	2016 £m
Trade receivables	**85**	85
Amounts owed by fellow subsidiaries of National Grid plc	**155**	7
Accrued income	**147**	288
Prepayments	**119**	57
Other receivables	**14**	9
	520	446

Provision for impairment of receivables	**2017** **£m**	2016 £m
At 1 April	**1**	4
Charge for the year	**-**	1
Amounts recovered in the year	**(1)**	-
Uncollectible amounts written off	**-**	(1)
Releases	**-**	(3)
At 31 March	**-**	1

Trade receivables past due but not impaired

	2017 **£m**	2016 £m
Up to 3 months past due	**5**	2
3 to 6 months past due	**-**	1
Over 6 months past due	**-**	1
	5	4

For further information about wholesale credit risk refer to note 25(a).

14. Financial and other investments

Financial and other investments include two main categories. Assets classified as available-for-sale typically represent investments in short-term money funds and quoted investments in equities or bonds of other companies. The second category is loans and receivables which includes bank deposits with a maturity of greater than three months, and cash balances that cannot be readily used in operations, principally collateral pledged for certain borrowings.

Financial assets, liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into, and recognised on trade date. Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any other categories.

Available-for-sale financial investments are recognised at fair value plus directly related incremental transaction costs, and are subsequently carried at fair value in the statement of financial position. Changes in the fair value of available-for-sale investments are recognised directly in other comprehensive income, until the investment is disposed of or is determined to be impaired. At this time the cumulative gain or loss previously recognised in equity is included in the income statement for the period. Investment income is recognised using the effective interest method and taken through interest income in the income statement.

Loans receivable and other receivables are initially recognised at fair value and subsequently held at amortised cost using the effective interest method. Interest income, together with gains and losses when the loans and receivables are derecognised or impaired, are recognised in the income statement.

Subsequent to initial recognition, the fair values of financial assets measured at fair value that are quoted in active markets are based on bid prices. When independent prices are not available, fair values are determined by using valuation techniques that are consistent with techniques commonly used by the relevant market. The techniques use observable market data.

	2017	2016
	£m	£m
Current		
Available-for-sale investments [1]	**1,632**	-
Loans and receivables - amounts due from fellow subsidiaries	**21**	21
Loans and receivables - restricted cash balances [2]	**203**	116
	1,856	137

1 The available-for-sale investments at 31 March 2017 solely relate to investments in short-term money funds.

2 Comprises collateral placed with counterparties with whom we have entered into a credit support annex to the ISDA Master Agreement.

Available-for-sale investments are recorded at fair value. Due to their short maturities the carrying value of loans and receivables approximates their fair value. The maximum exposure to credit risk at the reporting date is the fair value of the financial investments. For further information on our credit risk, refer to note 25(a). None of the financial investments are past due or impaired.

15. Cash and cash equivalents

Cash and cash equivalents include cash balances, together with short-term investments with an original maturity of less than three months that are readily convertible to cash.

Net cash and cash equivalents reflected in the cash flow statement are net of bank overdrafts, which are reported in borrowings.

The carrying amounts of cash and cash equivalents and bank overdrafts approximate their fair values.

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for periods varying between one day and three months, depending on the immediate cash requirements, and earn interest at the respective short-term deposit rates.

Net cash and cash equivalents held in currencies other than sterling have been converted into sterling at year-end exchange rates. For further information on currency exposures, refer to note 25(d).

	2017	2016
	£m	£m
Cash at bank and short-term deposits	**-**	-
Cash and cash equivalents excluding bank overdrafts	**-**	-
Bank overdrafts (note 16)	**(8)**	(7)
Net cash and cash equivalents	**(8)**	(7)

16. Borrowings

We borrow money primarily in the form of bonds, borrowings from fellow subsidiaries and bank loans. These are for a fixed term and may have fixed or floating interest rates or are linked to the retail price index (RPI). As indicated in note 11, we use derivatives to manage risks associated with interest rates and foreign exchange.

Our price controls require us to fund our networks with a certain ratio of debt to equity and, as a result, we have issued a significant amount of debt. As we continue to invest in our networks, the value of debt is expected to increase over time. To maintain a strong balance sheet and to allow us to access capital markets at commercially acceptable interest rates, we balance the amount of debt we issue with the value of our assets, and take account of certain other metrics used by credit ratings agencies.

Borrowings, which include interest-bearing and inflation linked debt and overdrafts are recorded at their initial fair value which normally reflects the proceeds received, net of direct issue costs less any repayments. Subsequently these are stated at amortised cost, using the effective interest method. Any difference between the proceeds after direct issue costs and the redemption value is recognised over the term of the borrowing in the income statement using the effective interest method.

	2017 **£m**	2016 £m
Current		
Bank loans	**529**	473
Bonds	**308**	125
Other loans	**1**	1
Borrowings from ultimate parent company	**-**	1,236
Bank overdrafts	**8**	7
	846	1,842
Non-current		
Bank loans	**490**	908
Bonds	**3,961**	5,865
Other loans	**189**	171
Borrowings from ultimate parent company	**-**	317
	4,640	7,261
Total	**5,486**	9,103

Total borrowings are repayable as follows:	**2017** **£m**	2016 £m
Less than 1 year	**846**	1,842
In 1 - 2 years	**470**	270
In 2 - 3 years	**226**	429
In 3 - 4 years	**8**	364
In 4 - 5 years	**893**	7
More than 5 years:		
by instalments	**51**	51
other than by instalments	**2,992**	6,140
	5,486	9,103

The fair value of borrowings at 31 March 2017 was £6,777m (2016: £10,267m). Where market values were available, fair value of borrowings (Level 1) was £2,149m (2016: £3,419m). Where market values were not available, the fair value of borrowings (Level 2) was £4,628m (2016: £6,848m), calculated by discounting cash flows at prevailing interest rates. The notional amount outstanding of the debt portfolio at 31 March 2017 was £5,454m (2016: £8,969m).

None of the Group's borrowings are secured by charges over assets of the Group.

Collateral is placed with or received from any counterparty where we have entered into a credit support annex to the ISDA Master Agreement once the current mark-to-market valuation of the trades between the parties exceeds an agreed threshold. Included in current bank loans is £527m (2016: £470m) in respect of cash received under collateral agreements.

At 31 March 2017, we had bilateral committed credit facilities of £350m (2016: £350m) of which £350m was undrawn (2016: £350m undrawn). All of the unused facilities at 31 March 2017 and 31 March 2016 were held as backup to commercial paper and similar borrowings.

17. Trade and other payables

Trade and other payables includes amounts owed to suppliers, tax authorities and other parties which are due to be settled within 12 months. The total also includes deferred income, which represents monies received from customers but for which we have not yet delivered the associated service. These amounts are recognised as revenue when the service is provided.

Trade payables are initially recognised at fair value and subsequently measured at amortised cost. Due to their short maturities, the fair value of trade and other payables approximates their book value.

	2017 £m	2016 £m
Trade payables	**240**	445
Amounts owed to fellow subsidiaries of National Grid plc	**237**	120
Deferred income	**20**	95
Social security and other taxes	**68**	79
Other payables	**49**	80
	614	819

18. Other non-current liabilities

Other non-current liabilities include deferred income which will not be recognised as income until after 31 March 2017. It also includes payables that are not due until after that date.

All other non-current liabilities are recorded at amortised cost. There is no material difference between the fair value and the carrying value of other non-current liabilities.

	2017 £m	2016 £m
Deferred income	**177**	1,047
Other payables	**12**	-
	189	1,047

19. Pensions and other post-employment benefit obligations

We have employees who are members of the National Grid UK Pension Scheme (Section B) which is a defined benefit scheme closed to new entrants. Membership of the National Grid YouPlan (YouPlan) defined contribution trust is offered to all new employees. YouPlan was launched in 2013 and under the rules of the plan, National Grid double matches contributions to YouPlan up to a maximum of 6% of employee salary. YouPlan is the qualifying scheme used for automatic enrolment and new hires are enroled into YouPlan.

The fair value of defined benefit scheme assets and present value of defined benefit obligations are updated annually in accordance with IAS 19 (revised).

During the year ended 31 March 2017, in order for the Gas Distribution business to be sold externally, the National Grid UK Pension Scheme was split into three sections. This has resulted in a change in National Grid Gas from recognising a pension charge for the year and recognising the scheme as if it were a defined contribution scheme to recognising a net pension asset on the statement of financial position and accounting as a defined benefit scheme.

Below we provide a more detailed analysis of the amounts recorded in the primary financial statements.

For the defined contribution plan, the Group pays contributions into a separate fund on behalf of the employee and has no further obligations to employees. The risks associated with this type of plan are assumed by the member.

For the defined benefit retirement scheme, members receive benefits on retirement, the value of which is dependent on factors such as salary and length of pensionable service. The Group underwrites both financial and demographic risks associated with this type of scheme.

The cost of providing benefits in a defined benefit scheme is determined using the projected unit method, with actuarial valuations being carried out at each reporting date by a qualified actuary. This valuation method is an accrued benefits valuation method that makes allowance for projected earnings.

The Group’s obligation in respect of the defined benefit pension scheme is calculated separately by projecting the estimated amount of future benefit payments that employees have earned for their pensionable service in the current and prior periods. These future benefit payments are discounted to determine the present value of the liabilities and the fair value of plan assets and any unrecognised past service cost is then deducted. The discount rate used is the yield at the valuation date on high-quality corporate bonds.

The Group takes advice from an independent actuary relating to the appropriateness of any key assumptions applied which include life expectancy of members, expected salary and pension increases, and inflation. It should be noted that comparatively small changes in the assumptions used may have a significant effect on the amounts recognised in the income statement and the statement of other comprehensive income and the net liability recognised in the statement of financial position.

Remeasurements of net retirement obligations are recognised in full in the period in which they occur in the statement of other comprehensive income.

Risks

The defined benefit pension obligations are exposed to the primary risks outlined below.

Liabilities are calculated using discount rates set with reference to yields on high-quality corporate bonds prevailing in the US and UK debt markets and will fluctuate as yields change. Scheme funds are invested in a variety of asset classes, principally: equities, government securities, corporate bonds and property. Consequently, actual returns will differ from the underlying discount rate adopted and therefore have an impact on the net balance sheet liability.

Changes in inflation will affect both current and future pension payments and are partially mitigated through investment in inflation matching assets and hedging instruments.

Longevity is also a key driver of liabilities and changes in expected mortality will have a direct impact on liabilities. The liabilities are, in aggregate, relatively mature which serves to mitigate this risk to some extent.

The scheme's investment strategy seeks to balance the level of investment return sought with the aim of reducing volatility and risk. In undertaking this approach reference is made both to the maturity of the liabilities and the funding level. A number of further strategies are employed to manage underlying risks, including liability matching asset strategies, diversification of asset portfolios, interest rate hedging and active management of foreign exchange exposure.

National Grid UK Pension Scheme

The last full actuarial valuation for the National Grid UK Pension Scheme (NGUKPS) was carried out at 30 September 2015. Based on long-term financial assumptions, the contribution rate agreed to meet future benefit accrual was 36% of pensionable earnings (currently 31% by employers and 5% by employees). In addition, payments are made to the scheme to cover administration costs and the Pension Protection Fund levy.

With effect from 1 January 2017, sectionalisation of the National Grid UK Pension Scheme was carried out as part of the disposal of Gas Distribution. The National Grid UK Pension Scheme was split into three sections, each of which are legally and actuarially separate. Section B is supported by NGG and Section A is supported by other companies within the National Grid Group. Section C is supported by Cadent. The figures shown within these financial statements cover Section B. The first actuarial valuation for Section B will be carried out at 31 March 2017. The fair value of plan assets as at 31 March 2017 was £5,851m and fair value of plan liabilities as at 31 March 2017 was £5,806m.

19. Pensions and post-employment benefit obligations (continued)

Section B of the National Grid UK Pension Scheme
National Grid Gas and the Trustees have agreed a schedule of contributions, under which payments of £30m plus an adjustment for RPI will be made in 2017/18 and will thereafter rise in line with RPI. National Grid Gas has established a security arrangement with a charge in favour of the Trustees. This amount may change over time or following changes to National Grid plc's credit rating. At 31 March 2017 the value of this was required to be £192m. This was provided via £200m in letters of credit. The assets held as security will be paid to Section B in the event that National Grid Gas plc (NGG) is subject to an insolvency event, if NGG is given notice of less than 12 months that Ofgem intends to revoke its licence under the Gas Act 1986, if NGG fails to make the required contributions in relation to Section B, if NGG's credit rating by two out of three specified agencies falls below certain agreed levels for a period of 40 days, or if NGG grants any charges over its assets other than where agreed with the Trustees. The assets held as security will be released back to National Grid Gas if the scheme moves into surplus. In addition, NGG will make a payment of £65m (increased in line with RPI) into Section B if NGG's credit rating by two out of three specified agencies falls below certain agreed levels for a period of 40 days.

The scheme ceased to allow new hires to join from 1 April 2002. A DC section of the scheme was offered for employees joining after this date, which has since been replaced by The National Grid YouPlan (YouPlan).

Actuarial information

When deciding on these assumptions we take independent actuarial advice. Comparatively small changes in the assumptions applied may have a significant effect on the overall deficit or surplus of a defined benefit scheme.

The National Grid UK Pension Scheme is funded with assets held in a separate trustee administered fund. The arrangements are managed by a trustee company with a board consisting of company and member appointed directors. The directors are required to manage the arrangements in accordance with local regulations and the arrangements' governing documents, acting on behalf of its beneficiaries.

The arrangements are subject to independent actuarial funding valuations at least every three years and following consultation and agreement with National Grid, the qualified actuary certifies the rate of employers' contribution, which, together with the specified contributions payable by the employees and proceeds from the scheme's assets, are expected to be sufficient to fund the benefits payable.

The results of 2015 actuarial variation for the NG UKPS are shown below:

Latest full actuarial valuation[1]	30 September 2015
Actuary	Willis Towers Watson
Market value of scheme assets at latest valuation	£16,551m
Actuarial value of benefits due to members	£18,176m
Market value as percentage of benefits	91%
Funding deficit	£1,625m
Funding deficit (net of tax)	£1,349m

1. Note the NG UKPS valuation as 30 September 2015 occurred prior to sectionalisation and so the figures above represent the entire scheme (including what are now Section A and Section C). All subsequent tables relate to Section B (unless stated).

	2017 £m
Amounts recognised in the statement of financial position	
Present value of funded obligations	**(5,806)**
Fair value of scheme assets	**5,851**
	45
Present value of unfunded obligations	**-**
Net defined benefit asset	**45**
Represented by:	
Assets	45
	45

19. Pensions and post-employment benefit obligations (continued)

Amounts recognised in the income statement and the statement of other comprehensive income	2017 £m
Included within operating costs	
Administration costs	**1**
Included within payroll costs	
Defined contribution scheme costs	**14**
Defined benefit scheme costs:	
Current service cost	**5**
Special termination benefit cost - redundancies	**1**
	21
Included within finance income and costs	
Interest cost	**1**
Total included in the income statement	**22**
Remeasurements of pension asset	**(134)**
Total included in the statement of other comprehensive income	**(134)**

Reconciliation of the net defined benefit asset/(liability)

	2017 £m
Opening defined benefit liability at 1 January 2017	**(89)**
Cost recognised in the income statement	**(8)**
Remeasurement effects recognised in the statement of other comprehensive income	**134**
Employer contributions	**8**
Closing net defined benefit asset	**45**

	2017 £m
Changes in the present value of defined benefit obligations (including unfunded obligations)	
Opening defined benefit obligations	**(5,878)**
Current service cost	**(5)**
Interest cost	**(37)**
Remeasurement of the defined benefit obligations	**51**
Special termination benefit cost - redundancies	**(1)**
Benefits paid	**64**
Closing defined benefit obligations	**(5,806)**
Changes in the fair value of scheme assets	
Opening fair value of scheme assets	**5,789**
Interest income	**36**
Return on assets greater than assumed	**83**
Administration costs	**(1)**
Employer contributions	**8**
Benefits paid	**(64)**
Closing fair value of scheme assets	**5,851**
Actual return on scheme assets	**119**
Expected contributions to defined benefit scheme in the following year	**50**

19. Pensions and post-employment benefit obligations (continued)

Asset allocations

Within the asset allocations below there is significant diversification across regions, asset managers, currencies and bond categories. No comparatives are provided as due to pension sectionalisation within the National Grid group which occurred on 1 January 2017, the scheme changed from being accounted for as a defined contribution scheme to a defined benefit scheme.

	2017 Quoted £m	2017 Unquoted £m	2017 Total £m
Equities	**798**	**237**	**1,035**
Corporate bonds	**1,657**	**-**	**1,657**
Government securities	**2,389**	**-**	**2,389**
Property	**-**	**294**	**294**
Diversified alternatives [1]	**-**	**299**	**299**
Other	**-**	**177**	**177**
Total	**4,844**	**1,007**	**5,851**

1 Includes return seeking non-conventional asset classes.

Target asset allocations

National Grid UK (Section B) Pension Scheme's investment strategy is formulated specifically in order to manage risk, through investment in diversified asset classes, including the use of liability matching assets and where appropriate through the employment of interest rate and inflation hedging instruments. The target asset allocation of the scheme as at 31 March 2017 is as follows:

	%
Equities	**18**
Other	**82**
Total	**100**

Actuarial assumptions

The following financial assumptions have been applied in assessing defined benefit liabilities.

	2017 %
Discount rate [1]	**2.4**
Rate of increase in salaries [2]	**3.5**
Rate of increase in RPI [3]	**3.2**

1 The discount rate for pension liabilities has been determined by reference to appropriate yields on high quality corporate bonds prevailing in the UK debt market at the reporting date.

2 A promotional scale has also been used where appropriate. The assumption stated is that relating to service prior to 1 April 2014. The assumption for the rate of increase in salaries for service after this date is 2.2%.

3 This is the key assumption that determines assumed increases in pensions in payment and deferment. The assumptions were 3.2% for increases in pensions in payment and 3.2% for increases in pensions in deferment.

There is no material difference between the actuarial assumptions as at 1 January 2017 and 31 March 2017.

For sensitivity analysis, see note 26.

Assumed life expectations for a retiree age 65.	2017 years
Today:	
Males	**22.8**
Females	**24.6**
In 20 years:	
Males	**25.0**
Females	**26.8**

20. Provisions

We make provisions when an obligation exists, resulting from a past event and it is probable that cash will be paid to settle it, but the amount of cash required can only be estimated.

The main estimates relate to environmental remediation and decommissioning costs for various sites we own or have owned, other provisions, and lease contracts we have entered into that are now loss making.

We are committed to the protection and enhancement of the environment. However, we have acquired, owned and operated a number of assets which have, during the course of their operations, created an environmental impact. Therefore we have a provision that reflects the expected cost to remediate these sites. Current operations will seldom result in new sites with significant expected costs being added to the provision.

Provisions are recognised where a legal or constructive obligation exists at the reporting date, as a result of a past event, where the amount of the obligation can be reliably estimated and where the outflow of economic benefit is probable.

Provision is made for decommissioning and environmental costs, based on future estimated expenditures, discounted to present values. An initial estimate of decommissioning and environmental costs attributable to property, plant and equipment is recorded as part of the original cost of the related property, plant and equipment.

Changes in the provision arising from revised estimates or discount rates or changes in the expected timing of expenditures that relate to property, plant and equipment are recorded as adjustments to their carrying value and depreciated prospectively over their remaining estimated useful economic lives; otherwise such changes are recognised in the income statement.

The unwinding of the discount is included within the income statement as a financing charge.

	Decommissioning £m	Environmental £m	Restructuring £m	Other £m	Total provisions £m
At 1 April 2015	71	59	26	54	210
Additions	2	4	3	6	15
Unused amounts reversed	(8)	-	(1)	(3)	(12)
Unwinding of discount	2	2	1	-	5
Utilised	(20)	(1)	(11)	(4)	(36)
At 31 March 2016	47	64	18	53	182
Additions	107	3	1	138	249
Unused amounts reversed	-	(19)	(1)	(3)	(23)
Unwinding of discount	-	1	-	-	1
Utilised	(10)	-	(15)	(3)	(28)
Disposal as a result of discontinued operations	(26)	(27)	-	(41)	(94)
At 31 March 2017	**118**	**22**	**3**	**144**	**287**

	2017 £m	2016 £m
Current	**133**	55
Non-current	**154**	127
	287	182

Decommissioning provision

The decommissioning provision represents expenditure relating to the demolition of gas and LNG storage facilities expected to be incurred until 2026.

During October 2016, following the sale of the Gas Distribution business, the company sold 78 surplus land sites to a number of fellow National Grid Group undertakings, recognising a gain on disposal of £109 million. A legal agreement was entered into with these National Grid Gas Group companies to demolish the non-operational gas holders on these sites, creating a constructive obligation for the Company. As a result a provision of £107 million has been recognised at 31 March 2017.

Environmental provision

The environmental provision represents the estimated restoration and remediation costs relating to old gas manufacturing sites owned by the Company (discounted using a real rate of 1.0%). Cash flows are expected to be incurred between 2017 and 2076.

A number of uncertainties affect the calculation of the provision including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. The provision incorporates our best estimate of the financial effect of these uncertainties, but future material changes in any of the assumptions could materially impact the calculation of the provision. The undiscounted amount of the provision at 31 March 2017 was £27m (2016: £87m), being the undiscounted best estimate of the liability having regard to these uncertainties.

Restructuring provision

The restructuring provision principally relates to business reorganisation costs in the UK and is expected to be incurred until 2019.

Other provisions

Other provisions at 31 March 2017 include £134m (2016: £nil) in respect of business set up costs and business restructuring costs. We expect the majority of this provision to be utilised within one year.

21. Share capital

Ordinary share capital represents the total number of shares issued.

Share capital is accounted for as an equity instrument. An equity instrument is any contract that includes a residual interest in the consolidated assets of the Company after deducting all its liabilities and is recorded at the proceeds received, net of direct issue costs, with an amount equal to the nominal amount of the shares issued included in the share capital account and the balance recorded in the share premium account.

	Number of shares 2017 millions	Number of shares 2016 millions	2017 £m	2016 £m
At 31 March 2016 and 2017 - ordinary shares of $1^{2}/_{15}$p each				
Allotted, called-up and fully paid	**3,944**	3,944	**45**	45

In line with the provisions of the Companies Act 2006, the Company amended its Articles of Association and ceased to have authorised share capital.

22. Net Debt

Net debt represents the amount of cash and financial investments held, less borrowings, overdrafts and related derivatives.

The movement in cash and cash equivalents is reconciled to movements in net debt.

(a) Reconciliation of net cash flow to movement in net debt

	2017 £m	2016 £m
Increase/(decrease) in cash and cash equivalents	**2**	(8)
Increase/(decrease) in financial investments	**1,719**	(246)
(Increase)/decrease in borrowings and related derivatives	**(947)**	403
Net interest paid on the components of net debt	**803**	168
Change in net debt resulting from cash flows	**1,577**	317
Changes in fair value of financial assets and liabilities and exchange movements	**(131)**	(16)
Net interest charge on the components of net debt	**(1,141)**	(233)
Disposal of Gas Distribution business	**4,051**	-
Other non-cash movements	**911**	-
Movement in net debt (net of related derivative financial instruments) in the year	**5,267**	68
Net debt (net of related derivative financial instruments) at the start of the year	**(8,452)**	(8,520)
Net debt (net of related derivative financial instruments) at the end of the year	**(3,185)**	(8,452)

Composition of net debt
Net debt is made up as follows:

	2017 £m	2016 £m
Cash, cash equivalents and financial investments	**1,856**	137
Borrowings and bank overdrafts	**(5,486)**	(9,103)
Derivatives	**445**	514
Total net debt	**(3,185)**	(8,452)

(b) Analysis of changes in net debt

	Cash and cash equivalents £m	Bank overdrafts £m	Net cash and cash equivalents £m	Financial investments £m	Borrowings £m	Derivatives £m	Total debt £m
At 1 April 2015	1	-	1	384	(9,349)	444	(8,520)
Cash flow	(1)	(7)	(8)	(247)	624	(52)	317
Fair value gains and losses and exchange movements	-	-	-	-	(69)	53	(16)
Interest charges	-	-	-	-	(302)	69	(233)
At 31 March 2016	-	(7)	(7)	137	(9,096)	514	(8,452)
Cash flow	-	2	2	1,713	112	(250)	1,577
Fair value gains and losses and exchange movements	-	-	-	-	(173)	42	(131)
Interest charges	-	-	-	6	(1,118)	(29)	(1,141)
Other non-cash movements	-	-	-	-	747	164	911
Disposal	-	(3)	(3)	-	4,050	4	4,051
At 31 March 2017	**-**	**(8)**	**(8)**	**1,856**	**(5,478)**	**445**	**(3,185)**
Balances at 31 March 2017 comprise:							
Non-current assets	-	-	-	-	-	813	813
Current assets	-	-	-	1,856	-	51	1,907
Current liabilities	-	(8)	(8)	-	(838)	(185)	(1,031)
Non-current liabilities	-	-	-	-	(4,640)	(234)	(4,874)
	-	**(8)**	**(8)**	**1,856**	**(5,478)**	**445**	**(3,185)**

23. Commitments and contingencies

Commitments are those amounts that we are contractually required to pay in the future as long as the other party meets their obligations. These commitments primarily relate to operating lease rentals and energy purchase agreements which, in many cases, extend over a long period of time. We also disclose any guarantees that companies have given, where we pledge assets against current obligations which will remain for a specific period.

Future capital expenditure

	2017 £m	2016 £m
Contracted for but not provided	**372**	561

Operating lease commitments

	2017 £m	2016 £m
Amounts due:		
Less than 1 year	**7**	14
In 1 - 2 years	**6**	11
In 2 - 3 years	**5**	9
In 3 - 4 years	**4**	8
In 4 - 5 years	**4**	5
More than 5 years	**9**	17
	35	64

Other commitments, contingencies and guarantees

The value of other commitments and guarantees at 31 March 2017 amounted to £31m (2016: £197m), including energy purchase commitments amounting to £25m (2016: £97m). Energy purchase commitments relate to contractual commitments to purchase electricity or gas that are used to satisfy physical delivery requirements to our customers or for energy that we use ourselves (i.e. normal purchase, sale or usage) and hence are accounted for as ordinary purchase contracts.

Parent Company loan guarantees on behalf of subsidiaries

The Company has guaranteed the repayment of principal sums, any associated premium and interest on specific loans due from its subsidiaries to third parties. At 31 March 2017, the sterling equivalent amounted to £992m (2016: £1,234m).

Amounts receivable under sublease arrangements

The total of future minimum sublease payments expected to be received under non-cancellable subleases is £1m (2016: £6m).

Litigation and claims

Through the ordinary course of our operations, we are party to various litigation, claims and investigations. We do not expect the ultimate resolution of any of these proceedings to have a material adverse effect on our results of operations, cash flows or financial position.

24. Related party transactions

A related party is a company or individual who also has an interest in us, for example a company that provides a service to us with a director who holds a controlling stake in that company and who is also a Director of National Grid Gas plc. The related parties identified include fellow subsidiaries, joint ventures, associated undertakings, investments and key management personnel.

The following significant transactions with related parties were in the normal course of business. Amounts receivable from and payable to related parties are due on normal commercial terms:

	2017 £m	2016 £m
Income:		
Goods and services supplied	**189**	16
Expenditure:		
Services received	**28**	21
Corporate services received	**14**	16
Charges in respect of pensions costs	**37**	61
Interest paid on borrowings from fellow subsidiaries	**7**	15
	86	113
Outstanding balances at 31 March in respect of income, expenditure and settlement of corporation tax:		
Amounts receivable	**169**	7
Amounts payable	**257**	120
Advances to parent (due within one year):		
At 31 March	**21**	21
Advances to parent (due after more than one year):		
At 31 March	**3,426**	5,609
Borrowings payable to fellow subsidiaries (amounts due within one year):		
At 31 March	**-**	1,236
Borrowings payable to fellow subsidiaries (due after more than one year):		
At 31 March	**-**	317

There were no advances to other related parties at 31 March 2017 (2016: nil)

Amounts receivable from or payable to related parties in respect of sales and expenditure are ordinarily settled one month in arrears. The advance to the parent due after more than one year is not interest bearing. Advances to and borrowings from fellow subsidiaries are repayable on demand and bear interest at commercial rates.

No amounts have been provided at 31 March 2017 (2016: £nil) and no expense has been recognised during the year (2016: £nil) in respect of bad or doubtful debts for related party transactions.

Details of guarantees provided in respect of related parties are provided in note 23.

Details of key management compensation are provided in note 2(c).

25. Financial risk management

Our activities expose us to a variety of financial risks including currency risk, interest rate risk, credit risk, capital risk and liquidity risk. Our risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential volatility of financial performance from these risks. We use financial instruments, including derivative financial instruments, to manage risks of this type.

This note describes our approach to managing risk, including an analysis of assets and liabilities by currency type and an analysis of interest rate category for our net debt. We are required by accounting standards to also include a number of specific disclosures, (such as a maturity analysis of contractual undiscounted cash flows) and have included these requirements below.

Risk management related to financing activities is carried out by a central treasury department under policies approved by the Finance Committee of the National Grid plc Board. The objective of the treasury department is to manage funding and liquidity requirements, including managing associated financial risks, to within acceptable boundaries. The Finance Committee provides written principles for overall risk management, as well as written policies covering specific areas such as foreign exchange risk, interest rate risk, credit risk, liquidity risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity.

We have exposure to the following risks, which are described in more detail below:

- credit risk;
- liquidity risk;
- interest rate risk;
- currency risk; and
- capital risk.

(a) Credit risk

We are exposed to the risk of loss resulting from counterparties' default on their commitments including failure to pay or make a delivery on a contract. This risk is inherent in our commercial business activities. We are exposed to credit risk on our cash and cash equivalents, derivative financial instruments, deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables and committed transactions.

Treasury credit risk

Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments. Our limits are managed by the central treasury department of National Grid.

As at 31 March 2016 and 2017, we had a number of exposures to individual counterparties. In accordance with our treasury policies, counterparty credit exposure utilisations are monitored daily against the counterparty credit limits. Counterparty credit ratings and market conditions are reviewed continually with limits being revised and utilisation adjusted, if appropriate. Management does not expect any significant losses from non performance by these counterparties.

Customer credit risk

Our principal commercial exposure is governed by the credit rules within the Uniform Network Code. These set out the level of credit relative to the regulatory asset value (RAV) for each credit rating. Our credit policies and practices are designed to limit credit exposure by collecting security deposits prior to providing utility services, or after utility service has commenced if certain applicable regulatory requirements are met. Collection activities are managed on a daily basis. Sales to retail customers are usually settled in cash, cheques, electronic bank payments or by using major credit cards. The utilisation of credit limits is regularly monitored and collateral is collected against these accounts when necessary. Management does not expect any significant losses of receivables that have not been provided for as shown in note 13.

25. Financial risk management (continued)

(a) Credit risk (continued)

Offsetting financial assets and liabilities

The following tables set out financial assets and liabilities which are subject to offset and to enforceable master netting arrangements or similar agreements. The tables show the amounts which are offset and reported net in the statement of financial position. Amounts which cannot be offset under IFRS, but which could be settled net under terms of master netting agreements if certain conditions arise, and with collateral received or pledged, are shown to present National Grid Gas's net exposure.

Financial assets and liabilities on different transactions are only reported net if the transactions are with the same counterparty, a legal right of offset exists and the cash flows are intended to be settled on a net basis.

Amounts which do not meet the criteria for offsetting on the statement of financial position but could be settled net in certain circumstances principally relate to derivative transactions under ISDA (International Swaps and Derivatives Association) agreements where each party has the option to settle amounts on a net basis in the event of default of the other party.

National Grid Gas has similar arrangements in relation to bank account balances and bank overdrafts; and trade payables and trade receivables which are subject to general terms and conditions. However, these balances are immaterial.

				Related amounts available to be offset but not offset in statement of financial position		
As at 31 March 2017	Gross carrying amounts £m	Gross amounts offset £m	Net amount presented in statement of financial position £m	Financial instruments £m	Cash collateral received/ pledged £m	Net amount £m
Assets						
Derivative financial instruments	864	-	864	(157)	(518)	189
	864	-	864	(157)	(518)	189
Liabilities						
Derivative financial instruments	(419)	-	(419)	157	201	(61)
	(419)	-	(419)	157	201	(61)
Total	445	-	445	-	(317)	128

				Related amounts available to be offset but not offset in statement of financial position		
As at 31 March 2016	Gross carrying amounts £m	Gross amounts offset £m	Net amount presented in statement of financial position £m	Financial instruments £m	Cash collateral received/ pledged £m	Net amount £m
Assets						
Derivative financial instruments	1,080	-	1,080	(428)	(460)	192
	1,080	-	1,080	(428)	(460)	192
Liabilities						
Derivative financial instruments	(566)	-	(566)	428	103	(35)
	(566)	-	(566)	428	103	(35)
Total	514	-	514	-	(357)	157

25. Financial risk management (continued)

(b) Liquidity risk

We determine our liquidity requirements by the use of both short-term and long-term cash flow forecasts. These forecasts are supplemented by a financial headroom analysis which is used to assess funding adequacy for at least a 24 month period and maintain adequate liquidity for a continuous 12 month period.

We believe our contractual obligations, including those shown in commitments and contingencies in note 23 can be met from existing cash and investments, operating cash flows and internal or external financing that we reasonably expect to be able to secure in the future, together with the use of committed facilities if required.

Our debt agreements and banking facilities contain covenants, including those relating to the periodic and timely provision of financial information by the issuing entity, and financial covenants such as maintaining current rating levels. Failure to comply with these covenants, or to obtain waivers of these requirements, could in some cases trigger a right, at the lender's discretion, to require repayment of some of our debt, and may restrict our ability to draw upon our facilities to access the capital markets.

The following is an analysis of the contractual undiscounted cash flows payable under financial liabilities and derivative assets and liabilities as at the reporting date:

At 31 March 2017	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due 3 years and beyond £m	Total £m
Non-derivative financial liabilities					
Borrowings	**(798)**	**(464)**	**(217)**	**(3,975)**	**(5,454)**
Interest payments on borrowings [1]	**(121)**	**(106)**	**(100)**	**(1,247)**	**(1,574)**
Other non-interest bearing liabilities	**(289)**	**(12)**	**-**	**-**	**(301)**
Derivative financial liabilities					
Derivative contracts - receipts	**143**	**450**	**457**	**102**	**1,152**
Derivative contract - payments	**(210)**	**(308)**	**(57)**	**(164)**	**(739)**
Total at 31 March 2017	**(1,275)**	**(440)**	**83**	**(5,284)**	**(6,916)**

At 31 March 2016	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due 3 years and beyond £m	Total £m
Non-derivative financial liabilities					
Borrowings	(1,756)	(263)	(417)	(6,533)	(8,969)
Interest payments on borrowings [1]	(203)	(189)	(175)	(2,238)	(2,805)
Other non-interest bearing liabilities	(525)	-	-	-	(525)
Derivative financial liabilities					
Derivative contract - receipts	104	196	406	654	1,360
Derivative contract - payments	(61)	(216)	(328)	(346)	(951)
Total at 31 March 2016	(2,441)	(472)	(514)	(8,463)	(11,890)

1 The interest on borrowings is calculated based on borrowings held at 31 March without taking account of future issues. Floating rate interest is estimated using a forward interest rate curve as at 31 March. Payments are included on the basis of the earliest date on which the Company can be required to settle.

25. Financial risk management (continued)

(c) Interest rate risk

Interest rate risk arises from our long-term borrowings. Borrowings issued at variable rates expose us to cash flow interest rate risk, partially offset by cash held at variable rates. Borrowings issued at fixed rates expose us to fair value interest rate risk.

Our interest rate risk management policy is to seek to minimise total financing costs (being interest costs and changes in the market value of debt) subject to constraints. We do this by using fixed and floating rate debt and derivative financial instruments including interest rate swaps, swaptions and forward rate agreements.

We hold some borrowings on issue that are inflation linked. We believe that these provide a partial economic offset to the inflation risk associated with our UK inflation linked revenues.

The table in note 16 (borrowings) sets out the carrying amount, by contractual maturity, of borrowings that are exposed to interest rate risk before taking into account interest rate swaps.

During 2017 and 2016, net debt was managed using derivative instruments to hedge interest rate risk as follows:

	2017				
	Fixed rate £m	**Floating rate £m**	**RPI £m**	**Other [1] £m**	**Total £m**
Financial investments	**-**	**1,835**	**-**	**21**	**1,856**
Borrowings	**(1,891)**	**(535)**	**(3,060)**	**-**	**(5,486)**
Pre-derivative position	**(1,891)**	**1,300**	**(3,060)**	**21**	**(3,630)**
Derivative effect	**1,549**	**(1,117)**	**13**	**-**	**445**
Net debt	**(342)**	**183**	**(3,047)**	**21**	**(3,185)**

	2016				
Cash and cash equivalents	-	-	-	-	-
Financial investments	-	116	-	21	137
Borrowings	(3,018)	(2,030)	(4,055)	-	(9,103)
Pre-derivative position	(3,018)	(1,914)	(4,055)	21	(8,966)
Derivative effect	1,836	(1,374)	52	-	514
Net debt	(1,182)	(3,288)	(4,003)	21	(8,452)

1 Represents financial instruments which are not directly affected by interest rate risk, including investments in equity or other non-interest bearing instruments.

(d) Currency risk

We are exposed to foreign exchange risk arising from non-sterling future commercial transactions and non-sterling recognised assets and liabilities.

Our policy for managing foreign exchange risk is to hedge contractually committed foreign currency cash flows over a prescribed minimum size. Where foreign currency cash forecasts are less certain, our policy is to hedge a proportion of the cash flows based on the probability of those cash flows occurring. Instruments used to manage foreign exchange transaction risk include foreign exchange forward contracts and foreign exchange swaps.

During 2017 and 2016, derivative financial instruments were used to manage foreign currency risk as follows:

	2017				
	Sterling £m	**Euro £m**	**Dollar £m**	**Other £m**	**Total £m**
Financial investments	**1,856**	**-**	**-**	**-**	**1,856**
Borrowings	**(4,015)**	**(226)**	**(906)**	**(339)**	**(5,486)**
Pre-derivative position	**(2,159)**	**(226)**	**(906)**	**(339)**	**(3,630)**
Derivative effect	**(995)**	**190**	**912**	**338**	**445**
Net debt position	**(3,154)**	**(36)**	**6**	**(1)**	**(3,185)**

	2016				
Financial investments	137	-	-	-	137
Borrowings	(7,498)	(210)	(1,041)	(354)	(9,103)
Pre-derivative position	(7,361)	(210)	(1,041)	(354)	(8,966)
Derivative effect	(1,075)	177	1,059	353	514
Net debt position	(8,436)	(33)	18	(1)	(8,452)

There was no significant currency exposure on other financial instruments, including trade receivables and payables, and other receivables and payables.

25. Financial risk management (continued)

(e) Capital risk management

The capital structure of the Group consists of shareholders' equity, as disclosed in the consolidated statement of changes in equity, and net debt (note 21). Our objectives when managing capital are: to safeguard our ability to continue as a going concern, to remain within regulatory constraints of our regulated operating company and to maintain an efficient mix of debt and equity funding thus achieving an optimal capital structure and cost of capital. We regularly review and manage the capital structure as appropriate in order to achieve these objectives.

Maintaining appropriate credit ratings for our regulated company is an important aspect of our capital risk management strategy and balance sheet efficiency. We monitor our balance sheet efficiency by regulatory asset value (RAV) gearing calculated as net debt expressed as a percentage of RAV, which indicates the level of debt employed to fund our regulated business. It is compared with the level of RAV gearing indicated by Ofgem as being appropriate for our business, at around 62.5 - 65%. The RAV gearing ratio at 31 March 2016 was 55%.

(f) Fair value analysis

The financial instruments included on the statement of financial position are measured at fair value. These fair values can be categorised into hierarchy levels that are representative of the inputs used in measuring the fair value. The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used.

	2017				2016			
	Level 1	**Level 2**	**Level 3**	**Total**	Level 1	Level 2	Level 3	Total
	£m	**£m**	**£m**	**£m**	£m	£m	£m	£m
Assets								
Available-for-sale investments	**1,632**	**-**	**-**	**1,632**	-	-	-	-
Derivative financial instruments	**-**	**864**	**-**	**864**	-	1,080	-	1,080
	1,632	**864**	**-**	**2,496**	-	1,080	-	1,080
Liabilities								
Derivative financial instruments	**-**	**(206)**	**(213)**	**(419)**	-	(493)	(73)	(566)
Total	**1,632**	**658**	**(213)**	**2,077**	-	587	(73)	514

Level 1: Financial instruments with quoted prices for identical instruments in active markets.

Level 2: Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are based directly or indirectly on observable market data.

Level 3: Financial instruments valued using valuation techniques where one or more significant inputs are based on unobservable market data.

Our level 3 derivative financial instruments include currency swaps where the currency forward curve is illiquid and inflation linked swaps where the inflation curve is illiquid. In valuing these instruments a third-party valuation is obtained to support each reported fair value.

The changes in value of our level 3 derivative financial instruments are as follows:

	2017	2016
	£m	£m
At 1 April	**(73)**	(68)
Net losses for the year [1]	**(11)**	(5)
Reclassification into level 3 [2]	**(129)**	-
At 31 March	**(213)**	(73)

1 Loss of £11m (2016: £5m loss) is attributable to derivative financial instruments held at the end of the reporting period and have been recognised in finance costs in the income statement.

2 Sterling RPI swaps reclassified from level 2 into level 3.

The impacts on a post-tax basis of reasonably possible changes in significant level 3 assumptions are as follows:

	2017 Income Statement	2016 Income Statement
	£m	£m
+ 20 basis points change in LPI market curve [1]	**(35)**	(31)
- 20 basis points change in LPI market curve [1]	**33**	30

1 A reasonably possible change in assumption of other level 3 derivative financial instruments is unlikely to result in a material change in fair values.

The impacts disclosed above were considered on a contract by contract basis with the most significant unobservable inputs identified.

26. Sensitivities on areas of estimation and uncertainty

In order to give a clearer picture of the impact on our results or financial position of potential changes in significant estimates and assumptions, the following sensitivities are presented. These sensitivities are hypothetical, as they are based on assumptions and conditions prevailing at the year end, and should be used with caution. The effects provided are not necessarily indicative of the actual effects that would be experienced because our actual exposures are constantly changing.

The sensitivities in the table below show the potential impact in the income statement (and consequential impact on net assets) for a range of different variables each of which have been considered in isolation (i.e. with all other variables remaining constant). There are a number of these sensitivities which are mutually exclusive and therefore if one were to happen, another would not, meaning a total showing how sensitive our results are to these external factors is not meaningful.

We are further required to show additional sensitivity analysis for changes in interest and exchange rates and these are shown separately in the subsequent table due to the additional assumptions that are made in order to produce meaningful sensitivity disclosures.

The sensitivities included in the table below all have an equal and opposite effect if the sensitivity increases or decreases by the same amount unless otherwise stated. For example a 10% increase in unbilled revenue at 31 March 2017 would result in an increase in the income statement of £15 million and a 10% decrease in unbilled revenue would have the equal but opposite effect.

	2017		2016	
	Income statement £m	**Net assets £m**	Income statement £m re-presented	Net assets £m re-presented
One year average increase in useful economic lives (pre-tax)				
Depreciation charge on property, plant and equipment	**6**	**6**	12	12
Amortisation charge on intangible assets	**4**	**4**	7	7
Estimated future cash flows in respect of provisions change of 10% (pre-tax)	**29**	**29**	18	18
Assets and liabilities carried at fair value change of 10% (pre-tax)				
Derivative financial instruments [1]	**45**	**45**	51	51
Unbilled revenue at 31 March change of 10% (post-tax)	**15**	**15**	29	29
No hedge accounting for our derivative financial instruments (post tax)	**(48)**	**(25)**	(7)	2

1 The effect of a 10% change in fair value assumes no hedge accounting.

Pensions obligations benefit (pre-tax) [2]	**2017 Income statement £m**	**2017 Net assets £m**
Discount rate change of 0.5% [3]	3	485
RPI rate change of 0.5% [4]	3	411
Change in long-term rate of increase in salaries change of 0.5% [5]	-	29
Change of one year to life expectancy at age 65	1	254

2 The changes shown are a change in the annual pension service charge and change in the defined benefit obligations. No comparatives are provided.

3 A change in the discount rate is likely to occur as a result of changes in bond yields and as such would be expected to be offset to a significant degree by a change in the value of the bond assets held by the scheme.

4 The projected impact resulting from a change in RPI reflects the underlying effect on pensions in payment, pensions in deferment and resultant increases in salary assumptions.

5 This change has been applied to both the pre 1 April 2015 and post 1 April 2015 rate of increase in salary assumption.

	2017		2016	
	Income statement £m	**Other equity reserves £m**	Income statement £m re-presented	Other equity reserves £m re-presented
Financial risk (post-tax)				
UK RPI rate change of 0.5% [1]	**12**	**-**	17	-
UK interest rate changes of 0.50%	**3**	**3**	12	26

1 Excludes sensitivities to LPI curve. Further details on sensitivities are provided in note 25 (f).

Financial instruments assumptions

Our financial instruments are sensitive to changes in market variables, being UK interest rates and the UK RPI. The changes in market variables impacts the valuation of our borrowings, deposits and derivative financial instruments. The analysis illustrates the sensitivity of our financial instruments to the changes in market variables.

The following main assumptions were made in calculating the sensitivity analysis for continuing operations:

- the amount of net debt, the ratio of fixed to floating interest rates of the debt and derivatives portfolio and the proportion of financial instruments in foreign currencies are all constant and on the basis of the hedge designations in place at 31 March 2017 and 2016 respectively;
- the statement of financial position sensitivity to interest rates relates only to derivative financial instruments and available-for-sale investments, as debt and other deposits are carried at amortised cost and so their carrying value does not change as interest rates move;
- the sensitivity of accrued interest to movements in interest rates is calculated on net floating rate exposures on debt, deposits and derivative instruments; and
- changes in the carrying value of derivatives from movements in interest rates of designated cash flow hedges are assumed to be recorded fully within equity.

27. Ultimate parent company

This note shows the immediate and ultimate parent companies for these consolidated financial statements.

National Grid Gas plc's immediate parent company is National Grid Gas Holdings Limited. The ultimate parent company and controlling party is National Grid plc. Both of these companies are incorporated in Great Britain and are registered in England and Wales. National Grid plc consolidates the financial statements of National Grid Gas plc. Copies of the consolidated financial statements of National Grid plc may be obtained from the Company Secretary, 1-3 Strand, London WC2N 5EH.

28. Subsidiary undertakings, and joint ventures

While we present consolidated results in these financial statements as if we were one company, our legal structure is such that there are a number of different operating and holding companies that contribute to the overall result. Our structure has evolved through acquisitions as well as regulatory requirements to have certain activities within separate legal entities.

Subsidiary undertakings
The list below contains all subsidiaries included within the National Grid Gas plc Group.

	Principal activity	Holding
British Transco Capital Inc. (incorporated in the US)	Financing	100%
British Transco Finance Inc. (incorporated in the US)	Financing	100%
British Transco International Finance BV (incorporated in the Netherlands)	Financing	100%
National Grid Metering Limited	Gas metering services	100%

Unless otherwise stated all subsidiaries are incorporated in England and Wales.

During the year ended 31 March 2017, as part of a group-wide restructuring exercise, National Grid Gas plc lost control of its majority stake in Xoserve Limited. National Grid Gas plc now holds 11% of the share capital of Xoserve Limited.

Joint ventures
The list below contains all joint ventures included within the National Grid Gas plc Group.

	Principal activity	Holding
Joint Radio Company Limited (incorporated in England and Wales)	Consultancy services	50%

Joint Radio Company Limited is based at 52 Dean Bradley House, Horseferry Road, London, SW1P 2AF.

Company accounting policies

for the year ended 31 March 2017

We are required to include the stand-alone balance sheet of our parent Company, National Grid Gas plc, under the Companies Act 2006, and the statement of changes of equity under Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"). The following disclosures provide additional information to stakeholders.

A. Basis of preparation of individual financial statements under FRS 102

National Grid Gas plc's principal activities involve the transmission and distribution of gas in Great Britain. The Company is a public limited company incorporated and domiciled in England, with its registered office at 1-3 Strand, London, WC2N 5EH.

These individual financial statements of the Company have been prepared in accordance with UK Accounting Standards, including FRS 102 and the Companies Act 2006.

The individual financial statements of the Company have been prepared on a historical cost basis, except for the revaluation of financial instruments, and are presented in pounds sterling, which is the currency of the primary economic environment in which the Company operates. The comparative financial information has also been prepared on this basis.

The individual financial statements have been prepared on a going concern basis following the assessment made by the Directors as set on page 38.

The Company has not presented its own profit and loss account as permitted by section 408 of the Companies Act 2006. The Company has taken advantage of the exemption, under FRS 102 paragraph 1.12(b), from preparing a cash flow statement.

The Company has also taken advantage of the exemption, under FRS 102 paragraph 1.12 (d), from making disclosures relating to share based payments as the equivalent disclosures are included in the consolidated financial statements of the Group, and also under paragraph 1.12(e), from disclosing transactions with other members of the National Grid group of companies.

In accordance with exemptions under FRS 102 paragraph 1.12(c), the Company has not presented the financial instruments disclosures required by the standard, as disclosures which comply with the standard are included in the consolidated financial statements.

B. Areas of judgement and key sources of estimation uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates. Information about such judgements and estimations is contained in the notes to the financial statements, and the key areas are summarised below.

Areas of judgement that have the most significant effect on the amounts recognised in the financial statements are as follows:

- environmental and decommissioning provisions – note 14.

Key sources of estimation uncertainty that have significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are consistent with those of the Group accounts, and are as follows:

- review of residual lives, carrying values and impairment charges for other intangible assets and property, plant and equipment – notes 4 and 5.
- estimation of asset/liabilities for pensions and other post-retirement benefits – notes 13.
- valuation of financial instruments and derivatives – notes 9.
- revenue recognition and assessment of unbilled revenue.
- environmental and decommissioning provisions – note 14.

C. Disposal of Gas Distribution

As described further in note 7 of the consolidated accounts, the disposal of the Gas Distribution business completed on 1 October 2016 and as a result all assets and liabilities of UK Gas Distribution were disposed.

As Gas Distribution represents a separate major line of business, the business is classified as a discontinued operation in the consolidated income statement. This has resulted in the re-presentation of comparative financial information in the income statement and statement of comprehensive income, split between continuing and discontinued operations.

D. Foreign currencies

Transactions in currencies other than the functional currency of the Company are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at closing exchange rates. Gains and losses arising on retranslation of monetary assets and liabilities are included in the profit and loss account.

E. Intangible assets

Computer software is stated at cost less accumulated amortisation and accumulated impairment losses. Software is amortised over the length of period we expect to receive benefit from the asset. The principal amortisation period for software is eight years.

Intangible assets are tested for impairment only if there is some indication that the carrying value of the assets may have been impaired. Impairments of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash generating unit to which that asset belongs is estimated. Impairments are recognised in the income statement and are disclosed separately. Any assets which suffered impairment in a previous period are reviewed for possible reversal of the impairment at each reporting date.

F. Tangible fixed assets

Tangible fixed assets are included in the balance sheet at their cost less accumulated depreciation. Costs include payroll costs and finance costs incurred which are directly attributable to the construction of tangible fixed assets, as well as the cost of any asset retirement obligations.

Tangible fixed assets include assets in which the Company's interest comprises legally protected statutory or contractual rights of use.

Additions represent the purchase or construction of new assets, including capital expenditure for safety and environmental assets, extensions to, enhancements to, or replacement of existing assets.

Contributions received towards the cost of tangible fixed assets from customers for connections to the gas transmission and distribution networks are initially recognised as deferred income and credited to revenue once the connection has been completed. Contributions received towards the provision of ongoing access to a supply of services are recognised initially as deferred income and revenue is subsequently recognised over the period in which the service is provided. Contributions received towards the altering, diverting or relocating a tangible fixed asset are included in creditors as deferred income and credited on a straight-line basis to the profit and loss account over the estimated useful economic lives of the assets to which they relate.

Depreciation is not provided on freehold land or assets in the course of construction. Other tangible fixed assets are depreciated on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives.

The assets' residual values are reviewed, and adjusted, if appropriate, at the end of each reporting period. The effect of any change is accounted for prospectively.

In assessing estimated useful economic lives, which are reviewed on a regular basis, consideration is given to any contractual arrangements and operational requirements relating to particular assets. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of tangible fixed assets are, in general, as shown in the following table:

Depreciation periods	Years
Freehold and leasehold properties	up to 50
Plant and machinery:	
– Mains, services and regulating equipment	30 to 100
– Meters and metering equipment	10 to 16
Motor vehicles and office equipment	up to 7

G. Fixed asset investments

Investments held as fixed assets are stated at cost less any provisions for impairment. Investments are reviewed for impairment if events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairments are calculated such that the carrying value of the fixed asset investment is the lower of its cost or recoverable amount. Recoverable amount is the higher of its net realisable value and its value-in-use, where value in use is the present value of future cash flows expected to be derived from an asset.

H. Impairment of fixed assets

Impairments of fixed assets are calculated as the difference between the carrying values of the net assets of income generating units, including where appropriate, investments, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken. Net realisable value represents the amount that can be generated through the sale of assets. Value in use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit.

Impairment reviews are carried out if there is some indication that impairment may have occurred, or where otherwise required to ensure that fixed assets are not carried above their estimated recoverable amounts. Impairments are recognised in the profit and loss account, and, where material, are disclosed as exceptional. Impairment reversals are recognised when, in management's opinion, the reversal is permanent.

I. Taxation

Current tax for the current and prior periods is provided at the amount expected to be paid or recovered using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or the right to pay less tax, at a future date, at tax rates expected to apply when the timing differences reverse, based on tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements.

Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

J. Stocks

Stocks are stated at cost less provision for deterioration and obsolescence. Cost is determined on the first-in, first-out (FIFO) method. Where applicable, cost comprises direct materials and direct labour costs as well as those overheads that have been incurred in bringing the stocks to their present location and condition.

K. Environmental costs

Environmental costs, based on discounted future estimated expenditures expected to be incurred, are provided for in full. The unwinding of the discount is included within the profit and loss account as a financing charge.

L. Revenue

Revenue represents the sales value derived from the transmission and distribution of gas and the provision of gas metering services during the year, including an assessment of services provided, but not invoiced as at the year end. It excludes value added tax and intra-company sales.

Where revenue for the year exceeds the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, a liability for the over- recovery is not recognised as such an adjustment to future prices relates to the provision of future services. Similarly, an asset is not recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under- recovery.

M. Pensions

The Company's employees are members of either the defined benefit National Grid UK Pension Scheme or the National Grid YouPlan defined contribution trust.

For defined benefit pension schemes, the regular service cost of providing retirement benefits to employees during the period, together with the cost of any benefits relating to past service, are recognised within operating costs.

The interest cost is calculated by applying the discount rate to the net balance of the defined benefit obligation and the fair value of plan assets. This cost is recognised in profit or loss account within net interest.

The present value of the defined benefit obligation, less the fair value of the assets of the scheme at the reporting date, is recognised on the balance sheet.

The difference between the actual and expected returns on scheme assets and the experience gains or losses arising on scheme liabilities, together with gains or losses arising from changes in actuarial assumptions, are charged or credited to other comprehensive income.

N. Leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. Operating lease payments are charged to the profit and loss account on a straight-line basis over the term of the lease.

O. Financial instruments

The Company’s accounting policies under FRS 102 are the same as the Group’s accounting policies under IFRS, namely IAS 32 ‘Financial Instruments: Presentation’, IAS 39 ‘Financial Instruments: Recognition and Measurement’ and IFRS 7 ‘Financial Instruments: Disclosures’. The Company applies these policies only in respect of the financial instruments that it has, namely investments, derivative financial instruments, debtors, cash at bank and in hand, borrowings and creditors.

The policies are set out in notes 6, 8, 9, 10, 11 and 12 to the consolidated financial statements. The Company is taking the exemption for financial instruments disclosures, because IFRS 7 disclosures are given in the notes to the consolidated financial statements.

P. Hedge accounting

The Company applies the same accounting policy as the Group in respect of fair value hedges and cash flow hedges. This policy is set out in note 11 to the consolidated financial statements.

Q. Share-based payments

National Grid issues equity-settled share-based payments to certain employees of the Company. Equity-settled share-based payments are measured at fair value at the date of grant, based on an estimate of the number of shares that will eventually vest. This fair value is recognised on a straight-line basis over the vesting period, as an operating cost and an increase in equity. Payments made by the Company to National Grid in respect of share-based payments are recognised as a reduction in equity.

R. Parent Company guarantees

The Company has guaranteed the repayment of the principal sum, any associated premium and interest on specific loans due from certain subsidiary undertakings to third parties. In the event of default or non-performance by the subsidiary, the Company recognises such guarantees as insurance contracts, at fair value with a corresponding increase in the carrying value of the investment.

S. Environmental provision

The environmental provision is calculated on a discounted basis and represents the estimated environmental restoration and remediation costs relating to a number of sites owned and managed by the Company.

T. Emission allowances

Emission allowances, which relate to the emissions of carbon dioxide, are recorded as an intangible asset within current assets and are initially recorded at cost, and subsequently at the lower of cost and fair value less costs to sell. For allocations of emission allowances granted by the UK Government, cost is deemed to be equal to fair value at the date of allocation.

Receipts of such grants are treated as deferred income and are recognised in the income statement in the period in which carbon dioxide emissions are made. A provision is recorded in respect of the obligation to deliver emission allowances and charges are recognised in the income statement in the period in which carbon dioxide emissions are made.

U. Dividends

Interim dividends are recognised when they are paid to the Company's shareholders. Final dividends are recognised in the financial year in which they are approved.

Company balance sheet

as at 31 March

	Notes	**2017 £m**	2016 £m
Fixed assets			
Intangible assets	4	**125**	239
Tangible assets	5	**4,358**	12,628
Investments	6	**17**	17
		4,500	12,884
Current assets			
Stocks and other current assets	7	**20**	26
Debtors (amounts falling due within one year)	8	**381**	469
Debtors (amounts falling due after more than one year)	8	**3,435**	5,650
Derivative financial instruments (amounts falling due within one year)	9	**51**	66
Derivative financial instruments (amounts falling due after more than one year)	9	**813**	1,014
Investments		**1,836**	117
Post employment benefits pension asset	13	**45**	-
		6,581	7,342
Creditors (amounts falling due within one year)	10	**(1,594)**	(2,819)
Net current assets		**4,987**	4,523
Total assets less current liabilities		**9,487**	17,407
Creditors (amounts falling due after more than one year)	11	**(4,949)**	(8,265)
Provisions for liabilities	14	**(668)**	(1,807)
Net assets		**3,870**	7,335
Capital and reserves			
Share capital	15	**45**	45
Share premium account		**204**	204
Cash flow hedge reserve		**(7)**	(61)
Capital redemption reserve		**1,332**	1,332
Profit and loss account		**2,296**	5,815
Total shareholders' equity		**3,870**	7,335

The Company financial statements set out on pages 91 to 100 were approved by the Board of Directors and authorised for issue on 30 June 2017. They were signed on its behalf by:

Nicola Shaw Chair

Alan Foster Director

National Grid Gas plc
Registered number: 2006000

Company statement of changes in equity

for the years ended 31 March

	Share capital £m	Share premium account £m	Profit and loss account £m	Cash flow hedge reserve £m	Capital redemption reserves £m	Total shareholders' equity £m
As at 1 April 2015	45	204	5,355	(56)	1,332	6,880
Profit for the year	-	-	1,074	-	-	1,074
Total other comprehensive loss for the year	-	-	-	(5)	-	(5)
Total comprehensive income/(loss) for the year	-	-	1,074	(5)	-	1,069
Equity dividends	-	-	(620)	-	-	(620)
Share-based payments	-	-	5	-	-	5
Tax on share-based payments	-	-	1	-	-	1
As at 31 March 2016	45	204	5,815	(61)	1,332	7,335
Profit for the year	-	-	4,464	-	-	4,464
Total other comprehensive income for the year	-	-	111	54	-	165
Total comprehensive income for the year	-	-	4,575	54	-	4,629
Equity dividends	-	-	(8,100)	-	-	(8,100)
Share-based payments	-	-	7	-	-	7
Tax on share-based payments	-	-	(1)	-	-	(1)
At 31 March 2017	**45**	**204**	**2,296**	**(7)**	**1,332**	**3,870**

The cash flow hedge reserve will be continuously transferred to the income statement until the borrowings are repaid. The amount due to be released from reserves to the income statement next year is £5m, and the remainder released with the same maturity profile as borrowings due after more than one year.

Other reserves comprise the capital redemption reserve arising from the refinancing and restructuring of the Lattice Group in 1999. It represents the amount of the reduction in the share capital of the Company as a consequence of that restructuring. As the amounts included in other reserves are not attributable to any of the other classes of equity presented, they have been disclosed as a separate classification of equity.

The Company is prohibited from declaring a dividend or other distribution unless it has certified that it is in compliance in all material respects with certain regulatory obligations, including a requirement to ensure it has sufficient financial resources and facilities to enable it to carry on its business and a requirement to use all reasonable endeavours to maintain an investment grade credit rating.

The Company has not presented its own profit and loss account and related notes as permitted by section 408 of the Companies Act 2006. The Company's profit after taxation was £4,464m (2016: £1,074m).

For further details of dividends paid and payable to shareholders, refer to note 6 in the consolidated financial statements.

Notes to the Company financial statements

1. Auditors' remuneration

Auditors' remuneration in respect of the Company is set out below:

	2017 £m	2016 £m
Audit services		
Audit fee of Company	**0.5**	0.3
Other services		
Fees payable to the company's auditors for audit-related assurance services	**0.2**	0.2
Other non audit services	**6.9**	7.7

Fees payable to the Company's auditors for audit-related assurance services represent fees payable for services in relation to engagements which are required to be carried out by the auditors. Other non audit services primarily includes amounts incurred in respect of the disposal of a majority stake in the Gas Distribution business (vendor due diligence and separation support). These fees have been subject to approval by the Audit Committee of National Grid plc.

2. Number of employees, including Directors

	2017 Monthly Average number	2016 Monthly Average number
Gas Transmission	**916**	878
Other	**829**	934
Total continuing	**1,745**	1,812
Discontinued - Gas Distribution [1]	**3,651**	3,608

1 Discontinued for 2017 represents the average number of employees employed for the six months prior to the Gas Distribution business being hived out on 1st October 2016.

Other comprises employees working in shared services supporting the Gas Transmission and Gas Distribution businesses.

3. Key management compensation

Key management comprises the Board of Directors of the Company together with those Executive Directors of National Grid plc who have managerial responsibility for National Grid Gas plc. Details of key management personnel compensation are provided in note 2(d) to the consolidated financial statements.

4. Intangible assets

	Software £m
Cost at 1 April 2016	602
Additions	24
Reclassifications [1]	3
Disposals	(7)
Disposal of discontinued operations	(298)
Cost at 31 March 2017	324
Accumulated amortisation at 1 April 2016	(363)
Amortisation charge for the year	(47)
Disposals	5
Disposal of discontinued operations	206
Accumulated amortisation at 31 March 2017	(199)
Net book value at 31 March 2017	**125**
Net book value at 31 March 2016	239

1 Represents amounts transferred from tangible assets (see note 5).

5. Tangible assets

	Land and buildings £m	Plant and machinery £m	Assets in the course of construction £m	Motor vehicles and office equipment £m	Total £m
Cost at 1 April 2016	444	19,547	224	546	20,761
Additions	10	319	132	22	483
Disposals	(21)	(247)	(5)	(111)	(384)
Disposal of discontinued operation	(61)	(11,612)	(21)	(251)	(11,945)
Reclassifications [1]	(11)	49	(61)	20	(3)
Cost at 31 March 2017	361	8,056	269	226	8,912
Accumulated depreciation at 1 April 2016	(220)	(7,456)	-	(457)	(8,133)
Depreciation charge for the year	(36)	(302)	-	(23)	(361)
Disposals	17	238	-	111	366
Disposal of discontinued operation	26	3,375	-	173	3,574
Accumulated depreciation at 31 March 2017	(213)	(4,145)	-	(196)	(4,554)
Net book value at 31 March 2017	**148**	**3,911**	**269**	**30**	**4,358**
Net book value at 31 March 2016	224	12,091	224	89	12,628

1 Represents amounts transferred between categories and also to intangible assets (see note 4).

The cost of tangible fixed assets at 31 March 2017 included £229m (2016: £224m) relating to interest capitalised. Interest was capitalised at the rate of 3.2% (2016: 3.2%)

The net book value of land and buildings comprised:

	2017 £m	2016 £m
Freehold	**88**	133
Short leasehold (under 50 years)	**60**	91
	148	224

Included within creditors (amounts falling due within one year) and creditors (amounts falling due after more than one year) are contributions to the cost of tangible fixed assets amounting to £nil (2016: £8m) and £31m (2016: £445m) respectively.

6. Investments

	Shares in subsidiary undertakings £m
Cost and net book value at 31 March 2016 and 31 March 2017	**17**

The names of the subsidiary undertakings and joint ventures are included in note 28 to the consolidated financial statements.

The Directors believe that the carrying value of the investments is supported by their underlying net assets.

7. Stocks and other current assets

	2017 £m	2016 £m
Raw materials and consumables	**18**	24
Other current assets - emission allowances	**2**	2
	20	26

8. Debtors

	2017 £m	2016 £m
Amounts falling due within one year:		
Trade debtors	**85**	84
Amounts owed by fellow subsidiary undertakings	**21**	37
Other debtors	**10**	6
Accrued income	**147**	286
Prepayments	**118**	56
	381	469
Amounts falling due after more than one year:		
Amounts owed by immediate parent undertaking [1]	**3,426**	5,609
Other debtors	**9**	41
	3,435	5,650
Total debtors	**3,816**	6,119

1 The amount owed by the parent is non-contractual.

The carrying values stated above are considered to represent the fair values of the assets.

9. Derivative financial instruments

The fair value of derivative financial instruments are:

	2017			2016		
	Assets £m	**Liabilities £m**	**Total £m**	Assets £m	Liabilities £m	Total £m
Amounts falling due within one year	**51**	**(185)**	**(134)**	66	(39)	27
Amounts falling due after more than one year	**813**	**(234)**	**579**	1,014	(527)	487
	864	**(419)**	**445**	1,080	(566)	514

For each class of derivative the notional contract amounts* are as follows:

	2017 £m	2016 £m
Interest rate swaps	**(3,173)**	(4,378)
Cross-currency interest rate swaps	**(728)**	(913)
Foreign exchange forward contracts	**(56)**	(46)
Inflation linked swaps	**(784)**	(762)
	(4,741)	(6,099)

*The notional contract amounts of derivatives indicate the gross nominal value of transactions outstanding at the balance sheet date.

For details on fair value techniques and assumptions, refer to note 25 to the consolidated financial statements.

10. Creditors (amounts falling due within one year)

	2017 £m	2016 £m
Derivative financial instruments (note 9)	**185**	39
Borrowings (note 12)	**953**	1,981
Trade creditors	**136**	297
Amounts owed to fellow subsidiary undertakings	**97**	119
Corporation tax	**9**	34
Other taxation and social security	**70**	78
Other creditors	**44**	73
Deferred income	**100**	198
	1,594	2,819

11. Creditors (amounts falling due after more than one year)

	2017 £m	2016 £m
Derivative financial instruments (note 9)	**234**	527
Borrowings (note 12)	**4,636**	7,252
Other creditors	**11**	-
Accruals and deferred income	**68**	486
	4,949	8,265

Deferred income mainly comprises contributions to capital projects.

12. Borrowings

The following table analyses the Company's total borrowings:

	2017 £m	2016 £m
Amounts falling due within one year:		
Bank loans and overdrafts	**539**	481
Bonds	**303**	120
Borrowings from subsidiary undertakings	**110**	143
Borrowings from ultimate parent company	**-**	1,236
Other loans	**1**	1
	953	1,981
Amounts falling due after more than one year:		
Bank loans	**490**	907
Bonds	**3,200**	5,000
Borrowings from subsidiary undertakings	**757**	857
Borrowings from ultimate parent company	**-**	317
Other loans	**189**	171
	4,636	7,252
Total borrowings	**5,589**	9,233

	2017 £m	2016 £m
Total borrowings are repayable as follows:		
Less than 1 year	**953**	1,981
In 1 - 2 years	**470**	270
In 2 - 3 years	**226**	221
In 3 - 4 years	**8**	364
In 4 - 5 years	**890**	7
More than 5 years by instalments	**51**	51
More than 5 years, other than by instalments	**2,991**	6,339
	5,589	9,233

The notional amount outstanding of the Company's debt portfolio at 31 March 2017 was £5,326m (2016: £8,731m).

None of the Company's borrowings are secured by charges over assets of the Company.

13. Pensions

Substantially all the Company's employees are members of either the defined benefit National Grid UK (Section B) pension scheme or the National Grid YouPlan defined contribution trust. The relevant information for both these schemes is included in note 19 to the consolidated financial statements.

The disclosures required by FRS 102 are the same as those required by IAS 19 (revised) and are provided in note 19 to the consolidated financial statements.

Amounts recognised in the balance sheet of the Company are as follows:

	2017 **£m**
Present value of funded obligations	**(5,806)**
Fair value of plan assets	**5,851**
	45
Net pension asset	**45**

Changes in the present value of defined benefit obligations (including unfunded obligations)	
Opening defined benefit obligations	**(5,878)**
Current service cost	**(5)**
Interest cost	**(37)**
Remeasurement of the defined benefit obligation	**51**
Special termination cost - redundancies	**(1)**
Benefits paid	**64**
Closing defined benefit obligations	**(5,806)**

Changes in the fair value of scheme assets	
Opening fair value of scheme assets	**5,789**
Interest income on plan assets	**36**
Return on plan assets greater than discount rate	**83**
Employer contributions	**8**
Administration costs	**(1)**
Benefits paid	**(64)**
Closing fair value of scheme assets	**5,851**

14. Provisions

	Decommissioning £m	Environmental £m	Restructuring £m	Deferred taxation £m	Other £m	Total £m
At 1 April 2016	47	65	20	1,623	52	1,807
Charged to profit and loss account	107	3	1	(150)	138	99
Transferred to reserves	-	-	-	36	-	36
Utilised	(10)	-	(16)	-	(3)	(29)
Released	-	(19)	(1)	-	(3)	(23)
Disposal of discontinued operation	(26)	(27)	-	(1,130)	(41)	(1,224)
Unwinding of discount	-	1	1	-	-	2
At 31 March 2017	**118**	**23**	**5**	**379**	**143**	**668**

Decommissioning provision

The decommissioning provision represents expenditure relating to the demolition of gas and LNG storage facilities expected to be incurred until 2020.

During October 2016, following the sale of the Gas Distribution business, the company sold 78 surplus land sites to a number of fellow National Grid Group undertakings, recognising a gain on disposal of £109 million. A legal agreement was entered into with these National Grid Gas Group companies to demolish the non-operational gas holders on these sites, creating a constructive obligation for the Company. As a result a provision of £107 million has been recognised at 31 March 2017.

Environmental provision

The environmental provision represents the estimated restoration and remediation costs relating to old gas manufacturing sites owned by the Company (discounted using a real rate of 1.0%). Cash flows are expected to be incurred between 2017 and 2077.

A number of uncertainties affect the calculation of the provision including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. The provision incorporates our best estimate of the financial effect of these uncertainties, but future material changes in any of the assumptions could materially impact the calculation of the provision. The undiscounted amount of the provision at 31 March 2017 was £27m (2016: £87m), being the undiscounted best estimate of the liability having regard to these uncertainties.

Restructuring provision

The restructuring provision principally related to business reorganisation costs and is expected to be incurred until 2019.

Deferred taxation

Deferred taxation comprises:

	2017 £m	2016 £m
Accelerated capital allowances	**382**	1,641
Other timing differences	**(3)**	(18)
	379	1,623

Other provisions

Other provisions at 31 March 2017 include £134m (2016: £nil) in respect of business set up costs and business restructuring costs. We expect the majority of this provision to be utilised within one year.

15. Share capital

	Number of shares 2017 millions	Number of shares 2016 millions	**2017 £m**	2016 £m
At 31 March 2016 and 2017 - ordinary shares of $1^{2}/_{15}$p each Allotted, called-up and fully paid	**3,944**	3,944	**45**	45

National Grid Gas plc is a wholly owned subsidiary undertaking of National Grid Gas Holdings Limited.

16. Commitments and contingencies

(a) Future capital expenditure

	2017 £m	2016 £m
Contracted for but not provided	**372**	553

(b) Operating lease commitments

	2017 £m	2016 £m
Amounts due:		
Not later than one year	**7**	13
Later than one year and not later than five years	**19**	29
Later than five years	**9**	12
	35	54

(c) Other commitments and contingencies

The value of other commitments, contingencies and guarantees at 31 March 2017 amounted to £31m (2016: £172m), including energy purchase commitments amounting to £25m (2016: £97m). Energy purchase commitments relate to contractual commitments to purchase electricity or gas that are used to satisfy physical delivery requirements to our customers or for energy that we use ourselves (i.e. normal purchase, sale or usage) and hence are accounted for as ordinary purchase contracts.

(d) Parent Company loan guarantees on behalf of subsidiary undertakings

The Company has guaranteed the repayment of principal sums, any associated premium and interest on specific loans due from its subsidiaries to third parties. At 31 March 2017, the sterling equivalent amounted to £992m (2016: £1,234m).

(e) Litigation and claims

Through the ordinary course of our operations, we are party to various litigation, claims and investigations. We do not expect the ultimate resolution of any of these proceedings to have a material adverse effect on our results of operations, cash flows or financial position.

17. Related parties

The following material transactions are with a former subsidiary of the Company which is not wholly owned by National Grid plc and are in the normal course of business. Other related party transactions are not disclosed in accordance with the exemptions available under FRS 102.

	2017 £m	2016 £m
Goods and services supplied	**78**	5
Services received	**16**	31
Amounts receivable at 31 March	**13**	-
Amounts payable at 31 March	**19**	1

Amounts payable or receivable are ordinarily settled one month in arrears. No amounts have been provided at 31 March 2017 (2016: £nil) and no expense has been recognised during the year (2016: £nil) in respect of bad or doubtful debts from the above related party transactions.

Glossary and definitions

References to the 'Company', 'we', 'our', and 'us', refer to National Grid Gas plc itself or to National Grid Gas plc and its subsidiaries collectively, depending on context.

EU
European Union

FRS
UK Financial Reporting Standard

GAAP
Generally accepted accounting principles

GHG
Greenhouse Gas

GW
Gigawatt, 10^9 watts

GWh
Gigawatt hours

HSE
Health and Safety Executive

IAS
International Accounting Standard

IASB
International Accounting Standards Board

IFRIC
International Financial Reporting Standards Interpretations Committee

IFRS
International Financial Reporting Standard

KPI
Key Performance Indicator

LNG
Liquefied natural gas

Lost time injury
A work-related injury which causes a person to be away from work for at least one normal shift after the shift on which the injury occurs, because the person is unfit to perform his or her duties

National Grid
National Grid plc, the ultimate parent Company of National Grid Gas plc and its controlling party

Ofgem
The Office of Gas and Electricity Markets

tonnes CO_2 equivalent
Measure of greenhouse gas emissions in relation to the impact of carbon dioxide

regulated controllable operating costs
Total operating costs under IFRS less depreciation and certain regulatory costs where, under our regulatory agreements, mechanisms are in place to recover such costs in current or future periods

regulatory asset value (RAV)
The value ascribed by Ofgem to the capital employed in the relevant licensed business. It is an estimate of the initial market value of the regulated asset base at privatisation, plus subsequent allowed additions at historical cost, less the deduction of annual regulatory depreciation. Deductions are also made to reflect the value realised from the disposal of certain assets that formed part of the regulatory asset base. It is also indexed to the RPI to allow for the effects of inflation

RIIO
The revised regulatory framework issued by Ofgem which was implemented in the eight year price controls which started on 1 April 2013

RoE
A performance metric measuring returns from the investment of shareholders' funds. It is a financial ratio of a measure of earnings divided by an equity base.
UK regulated return on equity is a measure of how a business is performing operationally against the the assumptions used by Ofgem. These returns are calculated using the assumption that the businesses are financed in line with the regulatory adjudicated capital structure, at the assumed cost of debt and that UK taxation paid is at the level assumed by Ofgem.

RPI
UK Retail Prices Index

TW
Terawatt, 10^{12} watts

TWh
Terawatt hours

National Grid Gas plc
1-3 Strand, London WC2N 5EH, United Kingdom