Annual Report and Accounts 2005/06
National Grid Electricity Transmission plc

Safety

Reliability

Efficiency

Responsibility

nationalgrid

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Business Review

Introduction

Overview of National Grid Electricity Transmission plc

The principal activities of National Grid Electricity Transmission plc (the "Company") are owner of the electricity transmission system in England and Wales and, as the Great Britain System Operator, managing the operations of both the England and Wales transmission system and also the two high voltage electricity transmission networks in Scotland. In addition we own and operate the UK based elements of the electricity interconnector between France and England as part of a joint arrangement with the French transmission operator, RTE.

History and development of the business

On the restructuring of the electricity industry in England and Wales in 1990, the Company assumed ownership and control of the transmission network and certain parts of the interconnectors with Scotland and France from the Central Electricity Generating Board.

In October 2002 the Company's then ultimate parent, National Grid Group plc, merged with Lattice Group plc to form National Grid Transco plc. Immediately following the merger, the Group combined the management of the Company's UK electricity and Transco's gas transmission operations. In July the name was changed to National Grid plc.

Background information

We own and operate electricity assets, which include approximately 4,500 miles of overhead line, about 415 miles of underground cable and some 337 substations at 240 sites in England and Wales. In addition we also operate the two high voltage transmission networks in Scotland. Day-to-day operation of the Great Britain electricity transmission system involves the continuous real-time matching of demand with generation output, ensuring the stability and security of the power system and the maintenance of satisfactory voltage and frequency.

External and regulatory environment

The electricity market in the UK is regulated by Ofgem, which has the responsibility for promoting competition, wherever appropriate, and for regulating the companies that own and operate the infrastructure through which electricity is delivered.

The functioning of the electricity market in Great Britain is governed by the British Electricity Trading and Transmission Arrangements, which became effective on 1 April 2005.

The Company is the sole holder of an electricity transmission licence for England and Wales. This licence also covers our role as the Great Britain System Operator. We have a duty under the Electricity Act 1989 to develop and maintain an efficient, coordinated and economical system of electricity transmission and to facilitate competition in the supply and generation of electricity. Charges to users of the transmission networks comprise two principal elements: Transmission Network Use of System charges in respect of the electricity transmission owner activity and Balancing Services Use of System charges in respect of the electricity system operator activity. We collect these charges from all Great Britain transmission network users and make payments to the owners of the Scottish transmission networks for the element of the Transmission Network Use of System charges that relate to their networks.

Ofgem sets price controls in respect of the amounts that can be charged by the owners and operators of the electricity infrastructure in the UK. The current price controls in respect of our electricity transmission owner and electricity system operator activities commenced on 1 April 2001 and were originally intended to continue until 31 March 2006, but have been extended to 31 March 2007. The next five year price control period for electricity activities are due to commence on 1 April 2007.

The electricity interconnector between England and France does not form part of our electricity transmission network and is separately regulated via a financial ring-fencing arrangement.

Business drivers

As electricity transmission owner, we own and maintain the physical assets, develop the networks to accommodate new connections and disconnections, and manage a programme of asset replacement and investment to ensure the long-term reliability of the network. As electricity system operator, we undertake a range of activities necessary for the successful delivery in real time of secure, reliable and efficient energy. This involves the continuous real-time balancing of supply and demand, involving balancing services that include commercial arrangements with market participants that enable electricity demand or generation output to be varied.

The principal business drivers for our UK electricity transmission activities include:

- the price controls set by Ofgem, which determine the prices that can be charged to users of the electricity transmission networks;
- capital investment, which drives the regulatory asset value, a key component in determining our allowed revenues under our price controls;
- our ability to operate reliably, and so to earn incentives for good performance and avoid penalties for poor performance;
- meeting regulatory targets for management of the electricity systems, generating incentives for good performance; and
- our ability to operate efficiently.

Business driver	Description
Price control	The charges that we can charge for access to our electricity transmission system are currently determined by a formula linked to retail price inflation (RPI). This is set at RPI -1.5%. This formula is based upon Ofgem's estimates of operating expenditure, capital expenditure and asset replacement together with an allowed rate of return. The current rate of return is set at a real pre-tax rate of 6.25% on our regulatory asset value for our electricity network. Our electricity regulatory asset value at 31 March 2006 is currently £5.6 billion (2005: £5.3 billion).
Reliability	We are subject to an incentive scheme based on the reliability of the electricity transmission network in England and Wales. This is based on achieving reliability in excess of 99.9999%. For 2006/07 there is the potential to earn additional revenue up to 1% if loss of supply is less than 248 MWh. For loss of supply in excess of 274 MWh up to a collar of 653 MWh we can potentially lose up to 1.5% of revenue.
Efficiency	Our electricity system operations have incentive schemes where if we operate our network more efficiently than Ofgem's forecasts then we can increase our revenue. Our electricity SO external incentive, the Balancing Services Incentive Scheme (BSIS) has historically been agreed on an annual basis. For the 2006/07 scheme, the Company decided not to accept Ofgem's proposals for the BSIS target. The Company considers that neither of Ofgem's external proposals offered an appropriate balance of risk and reward. Normal arrangements for the operation of the system and management of payments will continue, but without a financial incentive on the Company. The Company is at all times obligated under its Transmission Licence to operate the system in an economic and efficient manner.

Current and future developments

Licence

On 1 April 2005 we became responsible for operating the GB transmission system, setting charges and maintaining the charging statements for all transmission users in Great Britain. As a consequence, under the regulatory arrangements for BETTA the Anglo-Scottish interconnector (previously subject to separate commercial agreements outside the regulated business) is now subject to price control in the same manner as other network infrastructure which forms part of the regulated businesses of Scottish Power and National Grid.

Other

On 28 October 2005, the judicial review sought by Scottish Power of the Gas and Electricity Markets Authority's decision to approve the Great Britain Electricity Transmission Network Use of System charging methodology developed and proposed by National Grid and Ofgem was dismissed.

UK Electricity Market Developments

The UK is entering a period of changing supply patterns for electricity. The sources of electricity are shifting, with the Government's emphasis on combating climate change and encouragement of renewable generation.

We continue to work with the UK Government and Ofgem to make possible the necessary investments in the electricity transmission network to support the development of renewable energy projects. The final Transmission Investment for Renewable Generation proposals from Ofgem recognised the need to invest in networks to accommodate renewables. Funding costs for £108 million of investment will be allocated to our electricity transmission owner activity allowable revenue for the upgrade of the Anglo-Scottish interconnector (conditional on the satisfactory outcome of key planning consent issues in Scotland). At this time access has been sought by over 13 GW of renewable generation consisting of over 200 offers in Scotland. For England and Wales offers have been made to 5 GW of renewable generation.

Future Capital Investment

Investment in electricity transmission systems is, by its nature, variable and is largely driven by changing sources of supply and asset replacement requirements. The electricity transmission licence obliges us to provide connections and capacity upon request for users wishing to use the networks.

The bulk of the current electricity transmission network was installed during the 1960s and 1970s, with main plant asset lives typically of between 40 to 50 years. Over the next few years, we anticipate substantially increasing investment on replacing parts of our UK electricity network as these assets will be due for renewal.

This, together with work required to meet changing supply sources, means that the UK electricity transmission business will be embarking on a significant increase in investment and network renewal.

In order to meet the increasing programme of work, we have been exploring ways to work more efficiently and collaboratively with major suppliers and contractors to manage the increase in workload effectively.

Operating performance

The winter of 2005/06 saw demand from the electricity transmission network in England and Wales hit a peak of 53.73 GW. This slightly exceeded the previous year's peak of 53.29 GW.

The total amount of electricity transmitted for 2005/06 was 312,399 GWh compared with 308,305 GWh for 2004/05.

Our progress against our objectives during the year includes the following:

Objective	Performance
Safety	During 2005/06 there were 6 lost time injuries compared with 5 in 2004/05.
Reliability	Electricity transmission network reliability in 2005/06 was 99.99990%. This compared with 99.99998% in 2004/05. Our target reliability is 99.99990%. Average annual availability of our electricity network in 2005/06 was 95.09%. This compared with 95.3% in 2004/05. This reflects the increased amount of asset replacement activity to ensure the reliability of the network for years to come. System availability at winter peak demand was 97.9% in 2005/06 compared with 97.6% in 2004/05.
Improve financial performance/ efficiency	Total operating profit after exceptional items decreased from £583 million in 2004/05 to £549 million in 2005/06.
Invest for future growth	Capital investment in the replacement, reinforcement and extension of the electricity transmission systems in 2005/06 was £526 million, compared with £395 million in 2004/05. In 2005/06, 50% or £265 million of electricity transmission capital expenditure was related to asset replacement, reflecting the increasing need to replace transmission network assets, many of which were commissioned in the 1960s.

Financial performance

Group revenue for the year ended 31 March 2006 was £1,964m, compared with £1,422 million in 2004/05. The £542 million increase was due to higher incentivised costs associated with the Balancing Services Incentive Scheme (BSIS) of £214 million which flow through to revenue, the collection of Transmission use of system charges of £249 million under the new British Electricity Trading and Transmission Arrangements (BETTA) on behalf of the Scottish network owners, and beneficial timing and inflationary impacts on revenue collection.

Total operating profit, before exceptional items, for the year ended 31 March 2006 was £549 million, compared with £580 million in 2004/05.

Electricity transmission operating profit for the year ended 31 March 2006, before exceptional items, was £484 million, compared with £539 million in 2004/05. The £55 million reduction in operating profit was mainly as a result of an increase in transmission owner depreciation of £69 million due to higher accelerated depreciation associated with early asset write offs, asset relifing and an increase in core depreciation reflecting the ramp up in the capital programme; BSIS losses of £21m; partly offset by timing and inflationary impacts associated with electricity transmission revenue collection of £17 million; and higher internal incentive profits of £19m.

Interconnectors operating profit for the year ended 31 March 2006 was £63 million compared with £36 million in 2004/05 reflecting higher capacity auction income. Other businesses operating profit for the year ended 31 March 2006 was £2 million compared with £5 million in 2004/05.

Exceptional Items – No exceptional costs were charged to operating profit during the year ended 31 March 2006 (2005: £nil). In the year ended 31 March 2005 there was an exceptional profit on sale in respect of the disposal, on 22 November 2004, of rights to income from the hydroelectric power station at Kielder.

Interest – The net interest payable by the Group for the year ended 31 March 2006 was £139 million (2005: £79 million). This increase in net interest payable is primarily as a result of the reduction in group interest receivable following the settlement of a substantial part of the amounts owed to the Company by National Grid Holdings as part of the capital reduction scheme which occurred in March 2005.

Taxation – The Group's tax charge for the year ended 31 March 2006 was £118 million (2005: £142 million). The decrease of £24 million compared to the prior year is largely due to the reduction in profit before taxation of £93 million compared to 2004/05.

Employee numbers – The average number of employees during the year ended 31 March 2006 was 2,312 compared with 2,190 in the prior period, as a result of the ramp up in the capital programme.

Fixed assets
We own the freehold of the majority of all sites associated with our UK electricity transmission business in England and Wales. The remainder are held on long-term leaseholds. The electricity transmission business does not own any sites in Scotland.

Agreements with landowners or occupiers are required for the overhead lines and underground cables which make up our electricity network in England and Wales. The majority of agreements are in the form of terminable wayleaves. The remainder are in the form of perpetual easements under which rights have been granted in perpetuity in return for a lump sum payment. The sites at which we have electricity substations are split between freehold and leasehold. Of the leasehold sites, the large majority are substations located on the premises of generators and are held on long-term leases for nominal rental payments. Of the remaining sites, most are held as ground rents (market price payable for land only) from the respective landlords, who include electricity distribution companies.

Through the Company, we also own the freehold of our control centre in Berkshire. We also have major offices in Warwick (freehold) and Leeds (freehold).

Regulatory Asset Base
The Directors' calculation of the regulatory value (RAB value) of the Transmission activity at the end of March 2006 was £5,582 million, £1,181 million greater than the historic cost net assets value.

Safety
Our approach to safety and occupational health is set out in our Group Vision for Safety. This is underpinned by Group-wide policies and strategy statements that are available on our website. Our objectives are demanding but, we believe, achievable:

- zero injuries to the public as a direct result of our operations;
- zero work-related injuries and illness wherever we work in the world; and
- zero work-related ill health.

Overall our aim is to develop a culture in which acting safely becomes second nature.

Environment
We are committed to a year-by-year improvement in our environmental performance. Our Group-wide environmental policy sets out the key areas we are addressing, and we continue to implement environmental management systems certified to the international standard ISO 14001 to help us deliver improvements in these areas.

Electric and magnetic fields
National Grid recognises that there is some scientific evidence suggesting certain adverse health effects are linked to electric and magnetic fields. There is also evidence linking an increased risk of certain diseases to proximity to power lines although the cause is not clear. As a consequence there is public concern and we take these issues very seriously. The balance of evidence remains against both power-frequency and radio-frequency electric and magnetic fields causing ill health.

The World Health Organisation has classified power-frequency electric and magnetic fields as "possibly" carcinogenic. Our recently updated Public Position Statement on EMFs helps set the framework within which we continually assess the scientific evidence in this area, determine any implications for the way in which we conduct our business, and explain to society what the science is telling us.

In our operations, as a minimum we aim to comply with regulations, guidelines or practices relating to electric and magnetic fields in force. Where other companies, such as telecommunications operators, use our assets, we expect them similarly to comply with the relevant regulations, guidelines or practices.

Contaminated land
We continue to manage our inherited portfolio of potentially contaminated land. This contamination has mainly arisen from older electrical substations where there is a risk that the ground may have been contaminated with oil in the past through accidental spillage or leakage from equipment.

Financial outlook
The areas of main focus for the year to 31 March 2007 are to continue to invest in network reliability and system security and to take out unnecessary cost from the business wherever it arises.

Directors' report

for the year ended 31 March 2006

The Directors of National Grid Electricity Transmission plc ("the Company") present their report and the audited accounts for the year ended 31 March 2006. This report also contains references to the Company and its subsidiaries ("the Group"), the listed ultimate parent undertaking, National Grid plc, formerly National Grid Transco plc ("NG"), the Board of NG ("the NG Board") and to NG and its subsidiaries ("the NG Group") as appropriate.

Change of name

The Company changed its name to National Grid Electricity Transmission plc from National Grid Company plc, on 26 July 2005. On the same date, National Grid Transco plc changed its name to National Grid plc.

Principal activities

See Business Review on page 1.

Results and developments

See Financial Performance section in the Business Review.

Dividends

The Directors do not recommend the payment of a final dividend (2005: £1,100.0m). No ordinary dividends (2005: £1,450.0m) were paid during the year. Preference dividends amounting to £2.5m (2005: £2.5m) were paid or payable in relation to the year ended 31 March 2006.

International financial reporting standards

This is the first annual report in which we are presenting consolidated financial statements under International Financial Reporting Standards (IFRS) and accounting policies and comparative figures have been restated to comply with IFRS as detailed in the accounts. The parent company financial statements continue to be prepared in accordance with UK GAAP.

Directors

The Directors of the Company, who served throughout the year, are: -

A B Chapman
S J Holliday
S Lucas
Dr R J Urwin
N P Winser

Directors' interests

The interests of Directors, other than A B Chapman, who are also NG Directors, in National Grid plc shares at 31 March 2006, are disclosed in the NG Annual Report and Accounts.

The interests of A B Chapman in NG ordinary shares, are as follows:

	Employee Sharesave Scheme Options	Executive Share Options	Performance Share Plan Awards	Shares Beneficially Owned*
1 April 2005	4,314	86,413	40,797	20,303
Granted	–	–	16,887	–
Exercised	–	(7,984)	–	–
31 March 2006	4,314	78,429	57,684	23,829**

* Note: Includes shares acquired under the Share Matching scheme. Subject to retention of the shares acquired in accordance with the rules of the scheme, matching awards are exercisable by AB Chapman (totalling 6,991 shares, at 1 April 2005 and 7,078 at 31 March 2006) in addition to the above.

** On 1 August 2005 NG ordinary shares were subject to a 43 for 49 capital consolidation in conjunction with alternative elections involving its 65p per share return of capital. Options to ordinary shareholders also included a 'B share election', the rights of which are set out in the Circular to shareholders dated 6 June 2005. Following this, AB Chapman holds nil B shares.

At no time during the year has any Director had any material interest in a contract within the Group, being a contract of any significance in relation to the business of the Company or its subsidiaries.

Biographies

Roger Urwin (60)
Chairman

A Director of the Company since 1995, Roger Urwin is also Group Chief Executive of NG. He was previously Chief Executive of London Electricity plc and prior to this he held a number of appointments within the Central Electricity Generating Board before joining the Midlands Electricity Board as Director of Engineering. He is a Non-executive Director of Utilico Investment Trust plc and is a Fellow of the Royal Academy of Engineering. He has announced his intention to retire from National Grid at the end of 2006.

Nick Winser (45)
Nick Winser became the NG Group Director responsible for UK and US Transmission operations, and Chief Executive of National Grid Company plc, in April 2003. He was previously Chief Operating Officer of US Transmission for NG. Nick joined the Company in 1993, becoming Director of Engineering in 2001. Prior to this, he had been with PowerGen since 1991 as principal negotiator on commercial matters, having joined the Central Electricity Generating Board in 1983 where he served in a variety of technical engineering roles.

Steve Lucas (52)
Steve Lucas is also Group Finance Director of NG, following the merger of Lattice Group plc with National Grid Group plc in October 2002. He had been Executive Director, Finance of Lattice Group plc since its demerger from BG Group in 2000. Previously he was Treasurer of BG Group having joined British Gas plc in 1994. A Chartered Accountant, Steve Lucas worked in private practice in the City of London until 1983. He then joined Shell International Petroleum Company, occupying a number of finance management positions and treasury roles, including seven years in Africa and the Far East. Steve is also a Non-executive Director of Compass Group PLC.

Steve Holliday (49)
Steve Holliday is Group Chief Executive designate of NG, following the announcement of Roger Urwin's retirement, having become Group Deputy Chief Executive of NG on 1 April 2006. He was previously responsible for NG's UK Gas Distribution and Business Services. Before joining the Group in March 2001, he was an Executive Director of British Borneo Oil and Gas. Previously he spent 19 years with the Exxon Group, where he held senior positions in the international gas business and managed major operational areas such as refining and shipping. His international experience includes a four-year spell in the US. He also developed business opportunities in countries as diverse as China, Australia, Japan, Brazil and the former Soviet Union. Steve is also a Non-executive Director of Marks and Spencer Group plc.

Andy Chapman (49)
Andy Chapman is Finance Director, Transmission within NG and Finance Director of the Company, appointed in November 2004. Prior to this, he was NG Financial Controller following 5 years overseas in joint ventures where he spent 2 years as Chief Financial Officer, Intelig Telecomunicacoes, in Brazil and 3 years in Zambia working for the Copperbelt Energy Corporation occupying the position of Finance Director and, subsequently, Chief Executive Officer. He joined the Company in 1992 and is a qualified accountant.

Alison Kay
Company Secretary
Alison Kay has been Company Secretary since October 2002. She is also Company Secretary of National Grid Gas plc (formerly named Transco plc).

Corporate governance
National Grid is committed to the highest standards of corporate governance and the Board shares that commitment. The National Grid Group Annual Report and Accounts contains a detailed review of National Grid's arrangements.

Employee involvement
We have established, through e-mails, intranets, cascade briefings and in-house magazines, effective methods for communicating with employees on matters of concern to them. Regular consultation with staff and their trade union representatives takes place using both formal and informal mechanisms.

The Company remains committed to fair treatment of people with disabilities in relation to job applications, training, promotion and career development. Every effort is made to find appropriate alternative jobs for those who are unable to continue in their existing job due to disability.

The Company takes a positive approach to equality and diversity. We promote equality in the application of reward policies, employment and development opportunities, and aim to support employees in balancing work and personal lifestyles.

Employees are encouraged to become shareholders in NG and we operate a Sharesave Scheme and a Share Incentive Plan.

Pension arrangements
National Grid operates three major UK occupational pension schemes – the National Grid Electricity Group of the Electricity Supply Pension Scheme (the "National Grid Scheme"); the National Grid UK Pension Scheme (the "Lattice Scheme"); and the Crown Castle UK Pension Scheme (the "Crown Castle Scheme"). There are no current plans to merge the schemes.

The National Grid Scheme provides final salary defined benefits on a funded basis. The assets of the scheme are held in a separate trustee administered fund. The scheme is divided into sections, one of which is the National Grid section. It is subject to independent valuations at least every three years, on the basis of which 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 under the scheme. The last actuarial valuation of the National Grid Scheme, at 31 March 2004, was completed during the year ended 31 March 2005 and revealed a pre-tax deficit of £271.5m on the basis of the funding assumptions adopted by the actuary. Based on long-term financial assumptions the contribution rate required to meet future benefit accrual was 19.1% of pensionable earnings (13.1% employers and 6% employees). This contribution rate will be reviewed when the next independent actuarial valuation is carried out, which will be no later than 31 March 2007.

Research and development
Expenditure charged in 2005/06 on research and development was £2.5m (2005: £2.6m).

Payment to suppliers
The Company is a signatory to the CBI Code of Prompt Payment and has procedures to ensure the payment of bills in accordance with contractual terms. Copies of the CBI Code of Prompt Payment may be obtained from the CBI, Centre Point, 183 New Oxford Street, London WC1A 1DU.

The average creditor payment period at 31 March 2006 for the Company was 15 days (2005: 18 days).

Charitable and other donations
During the year, charitable donations of £300,000 (2005: £101,559) were made to UK charities, mainly in the area of the environment. In addition, the Company provides financial and in kind support to many other organisations through its community involvement programme.

No donations were made in the UK or EU for the purposes of the Political Parties Elections and Referendums Act 2000 (2005: £nil).

Treasury and financing
Both short and long-term cash flow forecasts are produced on a frequent basis to assist in identifying the liquidity requirements of the NG Group. In turn, the Group seeks to ensure that all of its forecast cash needs for a period of at least twelve months ahead are covered and maintains a minimum level of committed facilities in support of that objective.

The Company has access to sources of liquidity through a US$1.0bn US commercial paper programme (unutilised), a US$1.0bn Euro commercial paper programme (unutilised), a joint Euro medium term note programme with NG of €6.0bn (€2.0bn unissued), £450m long term and £25m short term of committed bank facilities (undrawn) and the ability to demand repayment of an inter-company loan. The bank facilities are being held as a backup to commercial paper issuance.

The Company has signed a loan agreement for £200m with the European Investment Bank which can be drawn before June 2007.

Treasury policy
The funding and treasury risk management of the Group is carried out by a central department operating under policies and guidelines approved by the NG Board. The Finance Committee of the NG Board is responsible for regular review and monitoring of treasury activity and for approval of specific transactions. NG has a Treasury department which raises all the funding for the Group and manages interest rate and foreign exchange rate risk.

The NG Group has separate financing programmes for each of the rated companies, which includes the Company. All funding is approved by the NG Finance Committee. In respect of its own activities, the Board has its own Finance Committee. The use of derivative financial instruments (derivatives) is controlled by policy guidelines set by the NG Board.

The Treasury department is not operated as a profit centre. Debt and treasury positions are managed in a non-speculative manner, such that all transactions in financial instruments or products are matched to an underlying current or anticipated business requirement.

The Company's financial position enables it to borrow on the wholesale capital and money markets and most of its borrowings are through public bonds and commercial paper. These borrowings contain no restrictive covenants.

The Group had borrowings, excluding derivatives, outstanding at 31 March 2006 amounting to £3,006.1m (2005: £3,088.9m).

NG places surplus funds on the money markets usually in the form of short-term fixed deposits which are invested with approved banks and counterparties. Details of the Group's short-term deposits are shown in note 19 to the financial statements.

The Company has a long term credit rating of A2 (negative outlook) and A (credit watch with negative implications) and short term ratings of P1 and A1 from Moody's and Standard & Poor's respectively. These ratings mean that the Company and the Group should have good access to the capital and money markets for future funding when necessary.

The main risks arising from the Group's financing activities are those risks associated with refinancing, interest rates, exchange rates and counterparty credit. The Board reviews and agrees policies for managing each risk and they are summarised below.

Risk management
Refinancing risk management
The NG Board principally controls refinancing risk by limiting the amount of financing obligations (both principal and interest) arising on borrowings in any financial year. This policy restricts the Group from having an excessively large amount of debt to refinance in a given time frame. During the year, a mixture of short-term debt and long-term debt was issued.

Interest rate risk management
The interest rate exposure of the Group arising from its borrowings and deposits is managed by the use of fixed and floating rate debt, interest rate swaps, swaptions and forward rate agreements. The Group's interest rate risk management policy is to seek to minimise total financing costs (i.e. interest costs and changes in the market value of debt) subject to constraints so that even with large movements in interest rates, neither the interest cost nor the total financing cost can exceed pre-set limits. Some of the bonds in issue are index-linked i.e. their cost is linked to changes in the UK Retail Price Index (RPI). The Board believes that these bonds provide a good hedge for revenues which are also RPI-linked under the price control formula.

Foreign exchange risk management
The Group has predominantly sterling assets and liabilities and cash flows, as swap instruments are in place to manage the currency risks on non-sterling denominated debt. The exposure to currency risk is therefore minimal.

Counterparty risk management
At the year end the Group had £23.9m (2005: £22.9m) of cash and deposits. The Group is exposed to the credit risk of the counterparties to these investments of surplus funds and from the use of derivatives. The Board has agreed a policy for managing such risk, which is controlled through credit limits, approvals and monitoring procedures.

Derivative financial instruments held for purposes other than trading
As part of its business operations, the Group is exposed to risks arising from fluctuations in interest rates. The Group uses derivatives to manage exposures of this type and as such they are a useful tool in reducing risk. The Group's policy is not to use derivatives for trading purposes. Derivative transactions can, to varying degrees, carry both counterparty and market risk.

The Group enters into interest rate swaps to manage the composition of floating and fixed rate debt, and so hedge the exposure of borrowings to interest rate movements. In addition, the Group enters into bought and written option contracts on interest rate swaps. These contracts are known as 'swaptions'. The Group also enters into foreign currency swaps to manage the currency composition of borrowings and so hedge the exposure to exchange rate movements. Certain agreements are combined foreign currency and interest rate swap transactions. Such agreements are known as cross-currency swaps.

The Group enters into forward rate agreements to hedge interest rate risk on short-term debt and money market investments. Forward rate agreements are commitments to fix an interest rate that is to be paid or received on a notional deposit of specified maturity, commencing at a future specified date.

Changes in debt
During the year, the Company raised £325m of new finance through seven long-term debt issues.

Going concern
The Board has reviewed the Group's budget and cash flow forecasts for the year ending 31 March 2007 and the outline projections for the four subsequent years. The Directors confirm that they have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, the Directors continue to adopt the going concern basis in preparing the Group's consolidated accounts.

Disclosure of relevant information to auditors
So far as the Directors are aware there is no relevant audit information of which the Company's auditors are unaware. The Directors have taken all steps they ought to have taken as Directors to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Auditors
A resolution for the re-appointment of PricewaterhouseCoopers LLP will be proposed at the Annual General Meeting.

Annual General Meeting
Notice of the NGET Annual General Meeting for 2006 will be issued separately to shareholders.

On behalf of the board

A B Kay
Company Secretary
16 May 2006

Registered Office
1-3 Strand
London
WC2N 5EH

Registered in England and Wales No. 2366977

Statement of Directors' responsibilities for preparing the accounts

The Directors are required by the Companies Act 1985 to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company and of the Group as at the end of the financial year and of the profit or loss of the Group for the financial year.

The Directors consider that in preparing the accounts (detailed in the following sections: Accounting Policies, Accounts, and Notes to the Accounts), the Company has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates and all applicable accounting standards have been followed.

The Directors have responsibility for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and of the Group and which enable them to ensure that the accounts comply with the Companies Act 1985.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors, having prepared the accounts, have requested the Auditors to take whatever steps and to undertake whatever inspections they consider to be appropriate for the purposes of enabling them to give their audit report.

Independent auditors' report to the members of National Grid Electricity Transmission plc

We have audited the group accounts (the "accounts") of National Grid Electricity Transmission plc for the year ended 31 March 2006 which comprise the group income statement, the group statement of recognised income and expense, the group balance sheet, the group cash flow statement and the related notes. These accounts have been prepared under the accounting policies set out therein.

We have reported separately on the parent company accounts of National Grid Electricity Transmission plc for the year ended 31 March 2006.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the accounts in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, 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.

We report to you our opinion as to whether the accounts give a true and fair view and have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors Report is not consistent with the accounts, if the Group has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited accounts. The other information comprises only the Directors' Report and the Business Review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion

In our opinion:

- the accounts give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 March 2006 and of its profit and cash flows for the year then ended;
- the accounts have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Directors' Report is consistent with the accounts.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Birmingham
16 May 2006

Notes:

(a) The maintenance and integrity of the National Grid Electricity Transmission plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the accounts since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of accounts may differ from legislation in other jurisdictions.

Group Accounting Policies

for the year ended 31 March 2006

(a) Basis of preparation of Group accounts

These Group accounts have been prepared in accordance with International Financial Reporting Standards ("IFRS") and IFRIC interpretations endorsed by the European Union (EU) and with those parts of the Companies Act 1985 applicable to companies reporting under IFRS. They are prepared on the basis of all IFRSs and Interpretations that are mandatory for periods ending 31 March 2006 and in accordance with applicable United Kingdom law and Article 4 of the IAS regulation. The 2005 comparative financial information has also been prepared on this basis, with the exception of certain standards, details of which are given below, for which comparative information has not been restated.

The Group's transition date to IFRS is 1 April 2004. The rules for first-time adoption of IFRS are set out in IFRS 1 'First-time adoption of International Financial Reporting Standards'. In preparing the Group's first IFRS accounts, these transition rules have been applied to the amounts reported previously under generally accepted accounting principles in the United Kingdom ("UK GAAP"). IFRS 1 generally requires full retrospective application of the Standards and Interpretations in force at the first reporting date. However, IFRS 1 allows certain exemptions in the application of particular Standards to prior periods in order to assist companies in the transition process. National Grid Electricity Transmission plc has elected to adopt IAS 32 and IAS 39 with effect from 1 April 2005, with no restatement of comparative information for the year to 31 March 2005. Accounting policy notes l) and m) explain the basis of accounting for financial instruments pre and post 1 April 2005.

In respect of the comparative financial information disclosed, IFRS 1 requires that estimates made under IFRS must be consistent with estimates made for the same date under UK GAAP except where adjustments are required to reflect any differences in accounting policies.

The Group accounts have been prepared on an historical cost basis, except for the revaluation of certain financial instruments from 1 April 2005 onwards.

A summary of the more important group accounting policies is set out below.

(b) Basis of consolidation

The Group accounts include the accounts of National Grid Electricity Transmission plc ("the Company") and all its subsidiary undertakings ("Group Undertakings") (note 30). The accounts of Group undertakings used for consolidation are made up to 31 March.

The results of subsidiaries acquired or disposed of during the year are included in the Group income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

(c) Segmental reporting

In addition to presenting the financial results and financial position in the accounts, we provide a breakdown of those results and balances into our business segments. The presentation of segment information is based on the management responsibilities that existed at 31 March 2006. Our business segments are electricity transmission, Interconnectors and Other activities. Our geographical segments reflect the Group's principal activities in the UK.

(d) Intangible assets

Identifiable intangible assets are recorded at cost less accumulated amortisation and any provision for impairment.

Internally generated intangible fixed 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 are amortised on a straight-line basis over their estimated economic useful lives. Amortisation periods for intangible assets are:

Amortisation periods for categories of intangibles	Years
Software	3 to 5

(e) Property, plant and equipment

Property, plant and equipment is recorded at cost or deemed cost at the date of transition to IFRS, less accumulated depreciation and any impairment losses. At the date of transition, the vast majority of assets were valued at depreciated cost, as adjusted for IFRS measurement changes, with some assets being measured at deemed cost.

Cost includes payroll and finance costs incurred which are directly attributable to the construction of property, plant and equipment.

Property, plant and equipment include assets in which the Group'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.

Contributions received towards the cost of property, plant and equipment are included in creditors as deferred income and credited on a straight-line basis to the income statement over the estimated useful lives of the assets to which they relate.

No depreciation is provided on freehold land and assets in the course of construction.

Other 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, 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 property, plant and equipment are, in general, as shown below.

Depreciation periods for category of assets	Years
Plant and machinery	
Transmission plant	
– Towers	40 or 60
– Substation plant, overhead lines and cables	40 or 50
– Overhead line spacers	20
– Protection, control and communication equipment	15 or 25
Cross-Channel link	15 to 60
Freehold and leasehold properties	up to 40
Motor vehicles and office equipment	3 or 5

(f) Impairment of assets

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

Recoverable amount is defined as the higher of fair value less costs to sell and estimated value in use at the date the impairment review is undertaken.

Value in use represents the present value of expected future cashflows, discounted using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cashflows have not been adjusted.

Impairments are recognised in the income statement and, where material, are disclosed separately.

(g) Taxation

Current tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

Deferred taxation and investment tax credits

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

Deferred tax liabilities are generally recognised for 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.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, 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 in which the liability is settled or the asset is realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is dealt with in equity.

The carrying amount of deferred tax assets is reviewed at each balance sheet 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 asset to be recovered. Unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that future taxable profit 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 Group intends to settle its current tax asset and liabilities on a net basis.

Investment tax credits are amortised over the economic life of the asset which gives rise to the credits.

(h) Inventories
Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs as well as those overheads that have been incurred in bringing the inventories to their present location and condition.

(i) Revenues
Revenues primarily represent the sales value derived from the transmission of electricity and the provision of related services. It excludes intra-Group and inter-company transactions and is stated net of value added tax.

Where revenues received or receivable exceed the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, no liability is recognised. Similarly no asset is recognised when a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

(j) Post-retirement benefits
For defined benefit retirement schemes, the cost of providing benefits is determined using the projected unit method, with actuarial valuations being carried out at each balance sheet date.

Current service cost is recognised in operating costs in the period in which the defined benefit obligation increases as a result of employee services.

Actuarial gains and losses are recognised in full in the period in which they occur in the Statement of Recognised Income and Expense.

Past service costs are recognised immediately to the extent that benefits are already vested. Otherwise such costs are amortised on a straight-line basis over the period until the benefits vest.

Settlements are recognised when the Group enters into a transaction that eliminates all further legal or constructive obligations for benefits under a scheme.

Curtailments are recognised when the Group is committed to a material reduction in the number of employees covered by a scheme.

The retirement benefit obligations recognised in the balance sheet represent the present value of the defined benefit obligations, as reduced by the fair value of the scheme assets.

The expected return on scheme assets and the unwinding of the discount on defined benefit obligations are recognised within interest income and expense respectively.

(k) Leases
Rentals under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Assets held under finance leases are recognised at their fair value on inception and depreciated over their useful economic lives. The corresponding liability is recognised as a finance lease obligation within borrowings. Rental payments are apportioned between finance costs and reduction in the finance lease obligation, so as to achieve a constant rate of interest.

(l) Financial Instruments
Financial assets, liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities and is recorded at the proceeds received, net of direct issue costs.

Trade receivables do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts. Trade payables are not interest bearing and are stated at their nominal value.

Loans receivable and other receivables are carried 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.

Other financial investments are initially measured at cost including transaction costs, but with effect from 1 April 2005 are subsequently carried at fair value. Changes in the fair value of investments classified at fair value through profit and loss are included in the income statement, while changes in the fair value of investments classified as available for sale are recognised directly in equity, until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the net profit or loss for the period.

Interest-bearing loans and overdrafts are recorded at the proceeds received, net of direct issue costs plus accrued interest less any repayments. Prior to 1 April 2005, accrued interest is presented as part of current liabilities and not combined with the principal amounts payable.

Derivative financial instruments are recognised initially at fair value, and are subsequently also measured at fair value. Changes in the fair value of derivative financial instruments are included in the income statement to the extent hedge accounting is not applied.

Subsequent to initial recognition, the fair values of financial instruments measured at fair value that are quoted in active markets are based on bid prices for assets held and offer prices for issued liabilities. When independent prices are not available, fair values are determined by using valuation techniques which refer to observable market data. These include comparison with similar instruments where market observable prices exist, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis using the effective interest rate method.

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets (being assets that necessarily take a substantial period of time to get ready for their intended use or sale) are added to their cost. Such additions cease when the assets are substantially ready for their intended use or sale. All other borrowing costs are recognised in the income statement in the period in which they are incurred.

(m) Hedge accounting and derivative financial instruments

The Group enters into both derivative financial instruments (“derivatives”) and non-derivative financial instruments in order to manage its interest rate and foreign currency exposures. The principal derivatives used include interest rate swaps, forward rate agreements, currency swaps, forward foreign currency contracts and interest rate swaptions.

All derivative transactions are undertaken, or maintained, with a view to providing a commercial hedge of the interest or currency risks associated with the Group’s underlying business activities and the financing of those activities.

With effect from 1 April 2005, derivatives are carried in the balance sheet at their fair value.

From 1 April 2005, the accounting policy for hedge accounting is as described below. Disclosures on the impact of implementing IAS 39 at 1 April 2005 are set out in note 2.

Changes in the carrying value of financial instruments that are designated and effective as hedges of future cash flows (“cash flow hedges”) are recognised directly in equity and any ineffective portion is recognised immediately in the income statement. Amounts deferred in equity in respect of cash flow hedges are subsequently recognised in the income statement in the same period in which the hedged item affects net profit or loss. Where a non-financial asset or a non-financial liability results from a forecasted transaction or a firm commitment being hedged, the amounts deferred in equity are included in the initial measurement of that non-monetary asset or liability.

Changes in the carrying value of financial instruments that are designated as hedges of the changes in the fair value of assets or liabilities (“fair value hedges”) are recognised in the income statement. An equal and opposite amount is recorded as an adjustment to the carrying value of hedged items, with a corresponding entry in the income statement, to the extent that the change is attributable to the risk being hedged and that the fair value hedge is effective.

Changes in the fair value of derivatives that do not qualify for hedge accounting are recognised in the income statement as they arise, within finance costs.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, or 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 net profit or loss. For fair value hedges the cumulative adjustment recorded to its carrying value at the date hedge accounting is discontinued is amortised to the income statement using the effective interest method.

If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the income statement immediately.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those host contracts and the host contracts are not carried at fair value with unrealised gains or losses reported in the income statement.

Prior to 1 April 2005, the Group adopted UK GAAP accounting principles for hedge accounting and for derivatives. Derivatives used for hedging purposes were not recorded on the balance sheet as assets or liabilities. Monetary assets and liabilities in foreign currencies were retranslated at hedged rates instead of closing rates.

As permitted by the provisions of IFRS 1, the comparative balance sheet and income statement for the year ended 31 March 2005 have not been restated to reflect the adoption of IAS 39 ‘Financial Instruments: Recognition and Measurement’.

(n) Restructuring costs
Costs arising from Group restructuring programmes primarily relate to redundancy costs. Redundancy costs are charged to the income statement in the year in which the Group becomes irrevocably committed to incurring the costs and the main features of the restructuring plan have been announced to affected employees.

(o) Employee benefit trusts
Shares held by employee benefit trusts are carried at cost less provision for impairment. Impairment is measured by reference to the option price of those shares required to settle outstanding options and by reference to market price, if applicable, for the remainder.

(p) Share-based payments
The Company’s ultimate parent company, National Grid plc, 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. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the ultimate parent company management’s estimate of shares that will eventually vest.

(q) Exceptional items
Exceptional items are credits or charges relating to non-recurring transactions that are material, significant or by their nature are relevant to understanding the Group’s financial performance and are shown separately to provide a better indication of the underlying results of the Group.

(r) Research and development
Research and development expenditure is charged to the income statement in the period in which it is incurred.

(s) Environmental costs
Provision is made for environmental costs, based on future estimated expenditures, but there is no discounting of any provision to present values.

(t) Foreign currencies
Transactions in currencies other than the functional currency of the Group undertaking concerned 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 income statement.

(u) Key sources of estimation uncertainty
The preparation of accounts 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 estimation is contained in the accounting policies and/or the Notes to the Accounts, and the key areas are summarised below.

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

- Review of residual lives, carrying values and impairment charges for intangible assets and property, plant and equipment – Group Accounting policies (d) Intangible assets, (e) Property, plant and equipment and (f) Impairment of assets
- Estimation of liabilities for post retirement benefits – note 8
- Valuation of financial instruments and derivatives – note 15
- Revenue recognition and assessment of unbilled revenues – Group accounting policies (i) Revenues
- Recoverability of deferred tax assets – Group accounting policies (g) Taxation and note 24
- Environmental liabilities – Group accounting policies (s) Environmental costs and note 22.

Group Income Statement

for the years ended 31 March

	Notes	**2006 £m**	2005(i) £m
Group revenue	3(a)	**1,964.1**	1,422.3
Operating costs	4	**(1,415.4)**	(839.5)
Operating profit			
– Before exceptional items and remeasurements	3(b)	**548.7**	580.1
– Exceptional items and remeasurements	5	**–**	2.7
Total operating profit	3(b)	**548.7**	582.8
Interest income and similar income	9	**107.2**	152.4
Interest payable and other finance costs	9	**(245.7)**	(231.7)
Profit before taxation			
– Before exceptional items and remeasurements		**409.6**	500.8
– Exceptional items and remeasurements	5	**0.6**	2.7
Total profit before taxation		**410.2**	503.5
Taxation			
– Before exceptional items and remeasurements	10	**(117.6)**	(141.8)
– Exceptional items and remeasurements §	5,10	**(0.2)**	–
Total taxation	10	**(117.8)**	(141.8)
Profit after taxation for the year			
– Before exceptional items and remeasurements		**292.0**	359.0
– Exceptional items and remeasurements	5	**0.4**	2.7
Profit after taxation for the year	26	**292.4**	361.7

All activities relate to continuing operations.

Group Statement of Recognised Income and Expense

for the years ended 31 March

	2006 £m	2005(i) £m
Actuarial gains on defined benefit pension schemes	**42.3**	43.9
Net losses taken to equity in respect of cash flow hedges	**(0.5)**	–
Share-based payment	**(1.5)**	–
Tax on items taken directly to equity	**(9.9)**	(12.2)
Net income recognised directly in equity	**30.4**	31.7
Profit for the year	**292.4**	361.7
Total income and expense for the year	**322.8**	393.4
Effect of change in accounting policy – IAS 39 (ii)	**(3.7)**	–
Total recognised income and expense for the year	**319.1**	393.4

(i) Refer to note 1 for the basis of preparation of the comparatives presented under International Financial Reporting Standards.
(ii) The Group has adopted IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' with effect from 1 April 2005, in accordance with the transition provisions of IFRS 1 (see note 2). An analysis of the impact that the adoption of IAS 32 and IAS 39 had on the Group's reserves is provided in note 26.

Group Balance Sheet

at 31 March

	Notes	2006 £m	2005(i) £m
Non-current assets			
Intangible assets	12	**76.0**	96.7
Property, plant and equipment	13	**4,520.3**	4,237.6
Other receivables	14	**23.4**	35.4
Derivative financial assets	15	**23.5**	–
Investments	16	**–**	28.0
Total non-current assets		**4,643.2**	4,397.7
Current assets			
Inventories	17	**15.8**	13.8
Trade and other receivables	18	**479.3**	580.2
Derivative financial assets	15	**15.7**	–
Cash and cash equivalents	19	**23.9**	22.9
Total current assets		**534.7**	616.9
Total assets	3(c)	**5,177.9**	5,014.6
Current liabilities			
Bank overdrafts	19	**(15.6)**	(18.0)
Borrowings	20	**(243.2)**	(458.4)
Derivative financial liabilities	15	**(8.5)**	–
Trade and other payables	21	**(763.6)**	(886.3)
Current tax liabilities		**–**	(0.2)
Provisions	22	**(2.9)**	(10.8)
Total current liabilities		**(1,033.8)**	(1,373.7)
Non-current liabilities			
Borrowings	20	**(2,747.3)**	(2,612.5)
Derivative financial liabilities	15	**(10.0)**	–
Other non-current liabilities	23	**(147.4)**	(89.2)
Deferred tax liabilities	24	**(700.0)**	(692.9)
Retirement benefit obligations	8	**(390.2)**	(422.0)
Provisions	22	**(17.2)**	(11.4)
Total non-current liabilities		**(4,012.1)**	(3,828.0)
Total liabilities	3(c)	**(5,045.9)**	(5,201.7)
Net assets/(liabilities)		**132.0**	(187.1)
Equity			
Called up share capital	25	**0.3**	0.3
Share premium account	26	**–**	–
Capital redemption reserve	26	**0.1**	0.1
Special reserve	26	**–**	–
Cash flow hedge reserve	26	**(7.9)**	–
Retained earnings	26	**139.5**	(187.5)
Total shareholders' equity/(deficit)	26	**132.0**	(187.1)

(i) Refer to note 1 for the basis of preparation of the comparatives presented under International Financial Reporting Standards.

These financial statements comprising the Group Income Statement, Group Statement of Recognised Income and Expense, Group Balance Sheet, Group Cash Flow Statement and the related notes 1 to 31, were approved by the Board of Directors on 16 May 2006 and were signed on its behalf by:

Nick Winser Director

Andy Chapman Director

Group Cash Flow Statement

for the years ended 31 March

	Notes	**2006 £m**	2005(i) £m
Cash flows from operating activities			
Total operating profit		**548.7**	582.8
Adjustments for:			
Exceptional items and remeasurements		**–**	(2.7)
Depreciation and amortisation	4	**269.4**	210.7
Share-based payment charge		**2.2**	–
Changes in working capital		**53.9**	(73.5)
Changes in provisions		**(2.1)**	(1.9)
Changes in post-retirement benefit obligations		**2.6**	3.0
Cash generated from operations		**874.7**	718.4
Tax paid		**(245.3)**	(179.9)
Net cash from operating activities		**629.4**	538.5
Cash flows from investing activities			
Acquisition of subsidiaries		**–**	(350.0)
Disposal of subsidiaries		**–**	350.0
Purchase of investments		**(7.1)**	(0.4)
Sale of investments		**32.6**	4.8
Purchases of intangible assets		**(1.8)**	(44.5)
Purchases of property, plant and equipment		**(473.6)**	(330.5)
Disposals of property, plant and equipment		**0.3**	4.4
Net cash used in investing activities		**(449.6)**	(366.2)
Cash flows from financing activities			
Increase in amounts due to Group undertakings		**116.4**	1,093.2
(Decrease)/increase in borrowings		**(148.5)**	240.5
Interest received		**31.4**	113.5
Interest paid		**(175.7)**	(171.3)
Equity dividends paid to shareholders		**–**	(1,450.0)
Net cash used in financing activities		**(176.4)**	(174.1)
Net increase/(decrease) in cash and cash equivalents	27(a)	**3.4**	(1.8)
Cash and cash equivalents at start of year (ii)		**4.9**	6.7
Cash and cash equivalents at end of year (ii)	19	**8.3**	4.9

(i) Refer to note 1 for the basis of preparation of the comparatives presented under International Financial Reporting Standards.
(ii) Net of bank overdrafts.

Notes to the Accounts

1. Adoption of International Financial Reporting Standards (IFRS)

With effect from 1 April 2005 National Grid Electricity Transmission plc (formerly National Grid Company plc) is required to report its consolidated accounts in accordance with IFRS. The tables below present the impact of conversion from UK generally accepted accounting principles (UK GAAP) to IFRS on the primary statements and selected notes. The transition date chosen for the adoption of IFRS is 1 April 2004, and only one year of IFRS comparatives are included in these accounts for the year ended 31 March 2006.

As permitted by International Financial Reporting Standard No. 1 'First-time Adoption of IFRS' (IFRS 1), the comparative balance sheet at 31 March 2005 and income statement for the year ended 31 March 2005 have not been restated to reflect the adoption of International Accounting Standard No. 39 'Financial Instruments: Recognition and Measurement' (IAS 39) on 1 April 2005. Summary disclosures on the impact of the adoption of IAS 39 and IAS 32 as at 1 April 2005 are included in note 2.

a) Impact of adoption of IFRS on net assets at 1 April 2004 (date of adoption of IFRS)

The following is a summary of the IFRS measurement and presentation adjustments as they affected net assets at 1 April 2004 (the date of adoption of IFRS), which arise as a consequence of applying IFRS measurement principles as compared with UK GAAP.

At 1 April 2004	Notes	£m
Net assets under UK GAAP		**885.1**
IFRS measurement adjustments		
BETTA	1(c)(i)	(4.6)
NETA	1(c)(ii)	(3.9)
Pensions	1(c)(iii)	(450.0)
Deferred taxation	1(c)(iv)	138.0
Proposed final dividend	1(c)(v)	350.0
Other	1(c)(vi)	(1.7)
IFRS presentation adjustments		
Reclassification of preference shares to current liabilities	1(d)(i)	(43.4)
Net assets under IFRS		**869.5**

Amounts shown above are net of any related deferred tax on the underlying IFRS adjustment.

b) Reconciliation of profit for the year and net assets under UK GAAP to IFRS

The following tables show the effect of IFRS measurement and presentation adjustments on profit for the year and net assets measured under UK GAAP as a consequence of applying IFRS measurement principles as compared with UK GAAP:

For the year ended 31 March 2005	Notes	£m
Profit for the year under UK GAAP		**361.2**
IFRS measurement adjustments		
BETTA	1(c)(i)	(7.8)
NETA	1(c)(ii)	1.0
Pensions	1(c)(iii)	11.3
Deferred taxation	1(c)(iv)	(1.4)
Other	1(c)(vi)	(0.1)
IFRS presentation adjustments		
Reclassification of preference share dividend to finance costs	1(d)(i)	(2.5)
Profit for the year under IFRS		**361.7**

Amounts shown above are net of any related deferred tax on the underlying IFRS adjustment.

1. Adoption of IFRS (continued)

b) Reconciliation of profit for the year end and net assets under UK GAAP to IFRS (continued)

At 31 March 2005	Notes	£m
Net assets under UK GAAP		**144.8**
IFRS measurement adjustments		
BETTA	1(c)(i)	(12.4)
NETA	1(c)(ii)	(2.9)
Pensions	1(c)(iii)	(394.8)
Deferred taxation	1(c)(iv)	123.4
Other	1(c)(vi)	(1.8)
IFRS presentation adjustments		
Reclassification of preference shares to current liabilities	1(d)(i)	(43.4)
Net liabilities under IFRS		**(187.1)**

Amounts shown above are net of any related deferred tax on the underlying IFRS adjustment.

c) IFRS measurement adjustments

The following relate to the measurement adjustments included in the income statement and balance sheet.

(i) British Electricity Transmission and Trading Arrangements (BETTA)

Certain BETTA costs under UK GAAP are included in debtors and then expensed to profit and loss over two years. Under IFRS, these costs cannot be deferred and are expensed in the year that they are incurred.

(ii) New Electricity Trading Arrangements (NETA)

NETA costs under UK GAAP are included in debtors and then expensed to profit and loss over seven years. Under IFRS, these costs cannot be deferred and are expensed in the year that they are incurred.

(iii) Pensions

Under UK GAAP, the Group's pensions were accounted for under SSAP 24. Under IFRS, these benefits are accounted for under IAS 19, with the Group recognising all of its net pension obligations in the balance sheet at 1 April 2004 with a corresponding adjustment to opening reserves. There are also differences in the measurement of the annual pension expense under IAS 19 compared with SSAP 24.

(iv) Deferred taxation

Under UK GAAP, deferred tax is recognised in respect of timing differences. Under IFRS, deferred tax is recognised in respect of temporary differences, being the differences between the book recorded value and the tax base of assets and liabilities. The adoption of IFRS resulted in a net reduction in the net deferred tax liability of £138.0m at 1 April 2004, principally reflecting the tax effect of the other IFRS adjustments recorded.

(v) Proposed final dividend

Under UK GAAP, final ordinary dividends were accounted for under SSAP 17 and recorded as a liability in the year in respect of which they were proposed by the Board of Directors for approval by the shareholders. Under IFRS, ordinary dividends are not provided until approved.

(vi) Other

Other differences on transition from UK GAAP to IFRS for the year ended 31 March 2005 are not individually material and relate principally to accrual of holiday pay.

d) IFRS presentation adjustments

The following notes relate to the presentation adjustments included in the income statement and balance sheet.

(i) Preference shares

Under UK GAAP, preference shares are shown as share capital and preference dividends are shown as dividends. Under IFRS, preference shares are classified as current liabilities and preference dividends are classified as finance costs.

(ii) Software

Under UK GAAP, software is capitalised together with the related hardware within property, plant and equipment. Under IFRS, software is classified within intangible assets.

1. Adoption of IFRS (continued)

d) IFRS presentation adjustments (continued)

(iii) Cash and cash equivalents

Under UK GAAP, cash excludes short-term highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant change in value. Under IFRS, such investments are included within cash and cash equivalents.

e) Impact of adoption of IFRS on the cash flow statement

The pre-tax cash flows from operations for the year ended 31 March 2005 were the same as those under UK GAAP. Other adjustments relate to changes in the categories: interest and dividend cash flows are now included within 'financing' instead of 'returns on investments and servicing of finance' and 'dividends paid' respectively, and 'capital expenditure and financial investment' and 'acquisitions and disposals' are now shown as one category, 'investing activities', instead of as two separate categories.

In accordance with IAS 7 'Cash flow statements', cash equivalents include certain bank deposits with a maturity of greater than 24 hours. These were previously shown as current asset investments, as they did not fall within the definition of cash according to UK GAAP. The effect of this classification was an £11.2m decrease in cash and cash equivalents cash flows for the year ended 31 March 2005 and an additional £0.8m being categorised as cash and cash equivalents in the balance sheet at 31 March 2005.

2. Adoption of IAS 39 and IAS 32 and presentation of net debt at 1 April 2005

a) Adoption of IAS 39 and IAS 32

On 1 April 2005 the Group adopted IAS 39 and IAS 32 acounting for financial instruments. IAS 39 requires certain financial instruments to be recorded in the balance sheet at fair value rather than historical cost. Note 15 contains the disclosures required by IAS 39 and IAS 32.

The principal effect of the adoption of these standards at 1 April 2005 is to record derivative financial instruments in the balance sheet at their fair value, while deferred gains and losses relating to items qualifying for hedge accounting are derecognised and instead recorded in equity (for cash flow hedges) or by adjusting the carrying value of the hedged financial instrument (for fair value hedges).

In accordance with IFRS 1, the balance sheet at 31 March 2005 and the income statement for the year ended 31 March 2005 have not been restated to reflect the adoption of IAS 39 and IAS 32 on 1 April 2005.

b) Effect of IAS 39 on net debt and net assets

	At 31 March 2005 £m	IAS 39 transition adjustment At 1 April 2005 (i), (ii), (iii) £m	IAS 39 reclass-ifications At 1 April 2005 £m	**IFRS post-IAS 39 At 1 April 2005 £m**
Cash and cash equivalents	**22.9**	–	–	**22.9**
Bank overdrafts	**(18.0)**	–	–	**(18.0)**
Net cash and cash equivalents	**4.9**	–	–	**4.9**
Borrowings	**(3,070.9)**	11.1	(38.4)	**(3,098.2)**
	(3,066.0)	11.1	(38.4)	**(3,093.3)**
Derivative financial assets	**–**	–	2.4	**2.4**
Derivative financial liabilities	**–**	(10.2)	10.2	**–**
Net debt	**(3,066.0)**	0.9	(25.8)	**(3,090.9)**
Accrued interest	**(27.9)**	2.1	25.8	**–**
Deferred gains and losses	**10.0**	(10.0)	–	**–**
Other assets and liabilities	**2,896.8**	3.3	–	**2,900.1**
Net liabilities	**(187.1)**	(3.7)	–	**(190.8)**

(i) On the adoption of IAS 39, derivative financial assets and liabilities are recognised on the balance sheet, with corresponding adjustments to retained earnings or to other reserves within equity (in respect of derivatives qualifying as cash flow hedges) or to the carrying value of debt (in respect of derivatives qualifying as fair value hedges). The impact on other assets and liabilities principally relates to the deferred tax effect of these adjustments.

(ii) Up to 31 March 2005, deferred gains and losses relating to hedged financial instruments were carried forward in the balance sheet and reflected in the profit and loss account in line with those hedged financial instruments. Under IAS 39, deferred gains and losses relating to qualifying hedge relationships are recorded in equity (for cash flow hedges) or by adjusting the carrying value of the hedged financial instrument (for fair value hedges) or in the income statement if hedge accounting is not achieved.

(iii) Up to 31 March 2005, accrued interest was presented separately within creditors from the financial instruments to which it relates. Under IAS 32 and IAS 39 the carrying value of borrowings and derivative financial assets and liabilities includes the related accrued interest balance.

3. Segmental analysis

Segmental information is presented in accordance with the management responsibilities and economic characteristics, including consideration of risks and returns, of the Group's business activities.

The following table describes the main activities for each business segment:

Electricity transmission	High-voltage electricity transmission networks
Interconnectors	French electricity interconnector
Other	Contracting activities and provision of support services

The Group assesses the performance of its businesses principally on the basis of operating profit before exceptional items and remeasurements.

Group revenue both in terms of origin and destination, profit, assets and liabilities are in respect of Europe.

a) Group revenue

	Total sales 2006 £m	**Sales between businesses 2006 £m**	**Sales to third parties 2006 £m**	Total sales 2005 £m	Sales between businesses 2005 £m	Sales to third parties 2005 £m
Continuing operations:						
Electricity transmission	**1,884.7**	**8.8**	**1,875.9**	1,366.0	28.9	1,337.1
Interconnectors	**77.0**	**0.4**	**76.6**	72.4	0.6	71.8
Other activities	**31.2**	**19.6**	**11.6**	29.1	15.7	13.4
	1,992.9	**28.8**	**1,964.1**	1,467.5	45.2	1,422.3

b) Operating profit

	Operating profit			
	Before exceptional items and remeasurements		After exceptional items and remeasurements	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Continuing operations:				
Electricity transmission	**483.6**	538.5	**483.6**	538.5
Interconnectors	**63.1**	36.4	**63.1**	36.4
Other activities	**2.0**	5.2	**2.0**	7.9
	548.7	580.1	**548.7**	582.8

c) Total assets and total liabilities

	Total assets		Total liabilities	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Continuing operations:				
Electricity transmission	**4,635.8**	4,306.2	**(551.2)**	(462.2)
Interconnectors	**101.7**	136.6	**(15.8)**	(9.1)
Other activities	**63.8**	93.5	**(35.8)**	(44.8)
Unallocated	**376.6**	478.3	**(4,443.1)**	(4,685.6)
	5,177.9	5,014.6	**(5,045.9)**	(5,201.7)

Unallocated total assets include cash and cash equivalents, taxation, derivative assets, investments in shares in the Group's ultimate parent undertaking, amounts owed by Group undertakings, and interest. Unallocated total liabilities include bank overdrafts, borrowings, derivative liabilities, taxation (including deferred taxation), amounts owed to Group undertakings, and interest.

3. Segmental analysis (continued)
d) Other segmental information

	Capital expenditure		Depreciation and amortisation	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Continuing operations:				
Electricity transmission	**529.8**	401.5	**259.6**	201.1
Interconnectors	**–**	0.4	**5.2**	6.0
Other activities	**1.9**	3.6	**4.6**	3.6
	531.7	405.5	**269.4**	210.7

Capital expenditure comprises additions to property, plant and equipment and other intangible assets amounting to £529.9m (2005: £361.0m) and £1.8m (2005: £44.5m) respectively.

Depreciation and amortisation includes depreciation of property, plant and equipment and amortisation of other intangible assets.

4. Operating costs

	2006 £m	2005 £m
Total operating costs comprise:		
Depreciation of property, plant and equipment	**246.9**	192.2
Amortisation of intangible assets	**22.5**	18.5
Payroll costs (note 6)	**88.8**	84.4
Other operating charges:		
– Rates	**94.1**	91.9
– Balancing Services Incentive Scheme direct costs	**537.0**	302.7
– Payments to Scottish network owners under BETTA	**258.9**	–
– Other non-exceptional operating charges	**167.2**	149.8
	1,057.2	544.4
	1,415.4	839.5
Operating costs include:		
Research expenditure	**2.5**	2.6
Operating lease rentals – land and buildings	**2.9**	2.7
Auditors' remuneration:		
Statutory audit services		
– Statutory audit fees	**0.4**	0.4
– Regulatory reporting	**0.1**	0.1

5. Exceptional items and remeasurements
The Group separately discloses items of income and expenditure relating to non-recurring transactions that are material, either by their nature or their size, that are relevant to an understanding of the Group's financial performance. These include exceptional income or charges that do not relate to the underlying financial performance of the Group and certain remeasurement gains or losses arising from movements in the carrying value of financial instruments, principally derivatives, that do not achieve hedge accounting.

	2006 £m	2005 £m
Exceptional items included within operating profit – Kielder sale (i)	**–**	2.7
Exceptional items included within finance costs – loss on repurchase of debt	**(2.2)**	–
Remeasurements – net gains on financial instruments included within finance costs (ii)	**2.8**	–
Total exceptional items and remeasurements before taxation	**0.6**	2.7
Tax on Kielder sale (i)	**–**	–
Tax credit on loss on repurchase of debt	**0.7**	–
Tax on financial instrument remeasurements (ii)	**(0.9)**	–
Tax on exceptional items and remeasurements	**(0.2)**	–
Total exceptional items and remeasurements	**0.4**	2.7

(i) The exceptional profit on sale of assets for the year ended 31 March 2005 was £2.7m (before and after taxation) in respect of the disposal, on 22 November 2004, of rights to income from the hydroelectric power station at Kielder. The exceptional profit represents the cash consideration received less the net book value of the assets.

(ii) Remeasurements – net gains on financial instruments represent mark-to-market movements in the fair value of financial instruments, primarily derivatives, that are held mainly for economic hedging purposes, but which do not achieve hedge accounting or are partly ineffective under IAS 39.

6. Payroll costs and employees

a) Payroll costs

	2006 £m	2005 £m
Wages and salaries	**93.3**	92.1
Social security costs	**9.5**	8.9
Other pension costs	**13.9**	12.4
Gross payroll costs	**116.7**	113.4
Less: amounts capitalised	**(27.9)**	(29.0)
Net payroll costs	**88.8**	84.4

b) Number of employees

31 March 2006 Number	Average 2006 Number	Average 2005 Number
2,335	**2,312**	2,190

The vast majority of the employees are employed either directly or indirectly in the transmission of electricity in the UK.

c) Key management compensation

	2006 £m	2005 £m
Salaries and short-term employee benefits	**1.1**	0.7
Post-employment benefits	**1.0**	0.7
Share-based payments	**0.4**	0.3
	2.5	1.7

The key management is defined as the Board of Directors.

7. Directors' emoluments

Total emoluments of the Directors of the Group for the year ended 31 March 2006 were as follows:

	2006 £000	2005 £000
Salaries and benefits	**561**	416
Performance related bonus	**467**	200
	1,028	616

The emoluments of the highest paid Director were £414,600 (2005: £213,800). The amount of accrued pension at 31 March 2006 for the highest paid Director was £516,000 (2005: £457,000). The highest paid Director exercised share options in respect of shares in National Grid plc (the ultimate parent undertaking) during the year (2005: none).

The Directors emoluments include amounts in respect of accrued bonus which had not yet been approved at the date of these accounts.

Four Directors (2005: one Director) exercised share options in National Grid plc during the year.

Retirement benefits at 31 March 2006 are accruing in respect of five Directors (2005: five Directors) under a defined benefit scheme.

There has been no other change in the beneficial interests of the Directors in the ordinary shares of National Grid plc between 1 April 2006 and 16 May 2006, except in respect of routine monthly purchases under the SIP.

Where relevant, emoluments are based upon an allocation of Group Directors' costs from National Grid plc.

8. Retirement benefit obligations

Substantially all of the Group's employees are members of the Electricity Supply Pension Scheme which is a defined benefit pension scheme.

The Electricity Supply Pension Scheme provides final salary defined benefits on a funded basis. The assets of the scheme are held in a separate trustee administered fund. The scheme is divided into sections, one of which is the Group's section. The Group's section of the scheme was closed to new entrants on 1 April 2006. It is subject to independent valuations at least every three years, on the basis of which the qualified actuary certifies the rate of employers' contributions, 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 under the scheme.

The latest actuarial valuation was carried out by Hewitt Bacon and Woodrow at 31 March 2004. The projected unit method was used and the principal actuarial assumptions adopted were that the annual rate of inflation would be 2.9% and that future real increases in pensionable earnings would be 1.0%. Investments held in respect of pensions before they became payable would average 3.8% real annual rate of return and investments held in respect of pensions after they became payable would average 2.8% real annual rate of return and that pensions would increase at a real annual rate of 0.1%. The aggregate market value of the scheme's assets was £1,110m and the value of the assets represented approximately 80.4% of the actuarial value of benefits due to members calculated on the basis of pensionable earnings and service at 31 March 2004 on an ongoing basis and allowing for projected increases in pensionable earnings. The results of the actuarial valuation carried out at 31 March 2004 showed that, based on long-term financial assumptions, the contribution rate required to meet future benefit accrual was 19.1% of pensionable earnings (13.1% employers and 6% employees). This contribution rate will be reviewed when the next independent actuarial valuation is carried out, which will be no later than 31 March 2007. The actuarial valuation revealed a pre-tax deficit of £271.5m (£190.1m net of tax) on the basis of the funding assumptions adopted by the actuary.

It has been agreed that no funding of the deficit identified in the 2004 actuarial valuation will need to be provided to the scheme until the outcome of the actuarial valuation at 31 March 2007 is known. At this point, the Group will pay the gross amount of any deficit up to a maximum of £67.5m (£47.3m net of tax) into the scheme. Until the 31 March 2007 actuarial valuation has been completed, the Group has arranged for banks to provide the trustees of the National Grid Scheme with letters of credit. The main conditions under which these letters of credit could be drawn relate to events which would imperil the interests of the scheme, such as National Grid Electricity Transmission plc, a Group undertaking, becoming insolvent or the Group failing to make payments into the fund.

The amounts recognised in the balance sheet are determined as follows:

	2006 £m	2005 £m
Present value of funded obligations	**(1,711.2)**	(1,571.8)
Fair value of plan assets	**1,334.1**	1,161.4
	(377.1)	(410.4)
Present value of unfunded obligations	**(13.1)**	(11.6)
Net liability in the balance sheet	**(390.2)**	(422.0)

The amounts recognised in the income statement are determined as follows:

	2006 £m	2005 £m
Current service cost	**16.5**	15.3
Interest cost	**83.6**	84.0
Expected return on plan assets	**(75.7)**	(74.0)
Curtailments/settlement (gains)/losses on redundancies	**(1.5)**	2.6
Special termination benefits on redundancies	**2.6**	–
Total in employee benefit cost	**25.5**	27.9
Actual return on plan assets	**244.1**	116.2

8. Retirement benefit obligations (continued)

	2006 £m	2005 £m
Changes in the present value of the defined benefit obligation:		
Opening defined benefit obligation	**1,583.4**	1,552.6
Current service cost	**16.5**	15.3
Interest cost	**83.6**	84.0
Actuarial losses/(gains)	**126.1**	(1.7)
Losses on curtailments	**1.9**	2.6
Employee contributions	**5.9**	5.7
Benefits paid	**(78.3)**	(75.1)
Net transfers out	**(7.1)**	–
Net decrease in liabilities from disposals	**(7.7)**	–
Closing defined benefit obligation	**1,724.3**	1,583.4
Changes in the fair value of plan assets:		
Opening fair value of plan assets	**1,161.4**	1,099.8
Expected return on plan assets	**75.7**	74.0
Actuarial gains	**168.4**	42.2
Employer contributions	**14.7**	14.8
Employee contributions	**5.9**	5.7
Benefits paid	**(78.0)**	(75.1)
Net transfers out	**(7.1)**	–
Net decrease in assets from disposals	**(6.9)**	–
Closing fair value of plan assets	**1,334.1**	1,161.4
Expected contributions to defined benefit plans in the following year	**12.3**	12.0

The major categories of plan assets as a percentage of total plan assets were as follows:

	2006 %	2005 %
Equities	**60.9**	59.9
Corporate bonds	**7.5**	9.4
Gilts	**22.0**	21.3
Property	**8.4**	8.4
Cash	**1.2**	1.0
Total	**100.0**	100.0

The principal actuarial assumptions used were:		
Discount rate	**4.9**	5.4
Expected return on plan assets	**6.4**	6.7
Rate of increase in salaries (i)	**3.9**	3.9
Rate of increase in pensions in payment and deferred pensions	**3.0**	3.0
Rate of increase in Retail Price Index	**2.9**	2.9

(i) A promotional age-related salary scale has also been used.

The expected long-term rate of return on assets has been set reflecting the price inflation expectation, the expected real return on each major asset class and the long-term asset allocation strategy adopted for each plan. The expected real returns on specific asset classes reflect historical returns, investment yields on the measurement date and general future return expectations, and have been set after taking advice from the scheme's actuaries. The long-term asset allocation for the Group's section of the Electricity Supply Pension Scheme is 63% equities, 30% bonds, 7% property and other.

9. Finance income and costs

	2006 £m	2005 £m
Pensions – expected return on scheme assets	**75.7**	74.0
Interest income from bank deposits	**8.2**	9.8
Interest receivable from group undertakings	**19.3**	63.9
Interest receivable on finance leases	**4.0**	4.7
Interest income and similar income	**107.2**	152.4
Pensions – interest on scheme liabilities	**(83.6)**	(84.0)
Interest on bank loans and overdrafts	**(21.4)**	(20.4)
Interest on other borrowings	**(165.8)**	(160.5)
Interest payable to group undertakings	**(7.8)**	(2.0)
Preference dividends	**(2.5)**	(2.5)
Less: interest capitalised	**32.6**	37.7
Interest payable	**(248.5)**	(231.7)
Net gains/(losses) on derivative financial instruments:		
On derivatives designated as fair value hedges	**6.2**	–
On derivatives designated as cash flow hedges	**(0.2)**	–
On derivatives not designated as hedges or ineligible for hedge accounting	**(3.2)**	–
Interest payable and other finance costs	**(245.7)**	(231.7)
Net finance costs	**(138.5)**	(79.3)

Interest on the funding attributable to assets in the course of construction was capitalised during the year at a rate of 5.85% (2005: 5.8%).

Preference dividends of 5.79 pence per preference share have been charged to the income statement for the year ended 31 March 2006 (2005: 5.76 pence per preference share).

Ineffectiveness on fair value hedges includes a net gain of £17m from derivatives designated as fair value hedges and a net loss of £11m from the fair value adjustments to the carrying value of debt. Net gains on derivatives designated as cash flow hedges includes net gains of £0.6m transferred from equity.

10. Taxation

Taxation on items charged/(credited) to the income statement

	2006 £m	2005 £m
Payable to group undertakings for the surrender of tax losses	**146.6**	134.5
Adjustments to corporation tax in respect of prior years (i)	**(29.3)**	11.9
Adjustments to amounts payable to group undertakings in respect of prior years	**–**	(3.2)
	117.3	143.2
Deferred tax: timing differences	**(23.9)**	17.3
Adjustment to deferred tax in respect of prior years	**24.4**	(18.7)
	0.5	(1.4)
Taxation	**117.8**	141.8
Comprising:		
Taxation – excluding exceptional items and remeasurements	**117.6**	141.8
Taxation – exceptional items and remeasurements (note 5)	**0.2**	–
	117.8	141.8

(i) The corporation tax adjustment in respect of prior years does not include anything that relates to exceptional items.

10. Taxation (continued)

Taxation on items charged/(credited) to equity

	2006 £m	2005 £m
Deferred tax credit on revaluation of cash flow hedges	**(0.1)**	–
Deferred tax credit on share-based payment	**(2.7)**	(1.0)
Deferred tax charge on actuarial gains/losses	**12.7**	13.2
Deferred tax charge/(credit) to equity for the year	**9.9**	12.2

The tax charge for the period is lower (2005: lower) than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	2006 £m	2005 £m
Profit before taxation		
Before exceptional items and remeasurements	**409.6**	500.8
Including exceptional items and remeasurements	**0.6**	2.7
Profit before taxation	**410.2**	503.5
Profit before taxation multiplied by the rate of corporation tax in the UK of 30% (2005: 30%)	**123.1**	151.1
Effects of:		
Adjustments in respect of current income tax of previous years	**(29.3)**	8.7
Adjustments in respect of deferred tax of previous years	**24.4**	(18.7)
Other	**(0.4)**	0.7
Total taxation	**117.8**	141.8
	%	%
At the effective income tax rate		
Before exceptional items and remeasurements	**28.8**	28.3
Including exceptional items and remeasurements	**28.7**	28.2

11. Dividends

The following table shows the dividends paid to equity shareholders:

	2006 £ (per ordinary share)	2005 £ (per ordinary share)	**2006 £m**	2005 £m
Ordinary dividends				
Final dividend for the year ended 31 March 2004	**–**	10,982	**–**	350.0
Final dividend for the year ended 31 March 2005	**–**	342	**–**	1,100.0
			–	1,450.0

No dividend is proposed for 2006. The 2005 final dividend per share figure was based on 3,218,870 10p ordinary shares and the 2004 final dividend per share figure was based on 31,870 20p ordinary shares.

12. Intangible assets

	Software £m	Total £m
Cost at 1 April 2004	96.0	96.0
Additions	44.5	44.5
Disposals	(9.1)	(9.1)
Cost at 31 March 2005	131.4	131.4
Additions	1.8	1.8
Cost at 31 March 2006	133.2	133.2
Amortisation at 1 April 2004	25.3	25.3
Amortisation charge for the year (note 4)	18.5	18.5
Disposals	(9.1)	(9.1)
Amortisation at 31 March 2005	34.7	34.7
Amortisation charge for the year (note 4)	22.5	22.5
Amortisation at 31 March 2006	57.2	57.2
Net book value at 31 March 2006	**76.0**	**76.0**
Net book value at 31 March 2005	96.7	96.7

13. Property, plant and equipment

	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 2004	100.9	5,520.6	651.8	94.3	6,367.6
Additions	0.6	3.3	351.1	6.0	361.0
Disposals	(0.3)	(9.9)	–	(7.4)	(17.6)
Reclassifications	54.5	353.9	(413.9)	5.5	–
Cost at 31 March 2005	155.7	5,867.9	589.0	98.4	6,711.0
Additions	1.0	2.3	521.0	5.6	529.9
Disposals	(3.3)	(32.0)	–	(4.3)	(39.6)
Reclassifications	0.3	450.6	(455.4)	4.5	–
Cost at 31 March 2006	153.7	6,288.8	654.6	104.2	7,201.3
Depreciation at 1 April 2004	15.2	2,196.8	–	85.1	2,297.1
Depreciation charge for the year	3.1	179.0	–	10.1	192.2
Disposals	(0.2)	(9.9)	–	(5.8)	(15.9)
Reclassifications	19.5	(18.2)	–	(1.3)	–
Depreciation at 31 March 2005	37.6	2,347.7	–	88.1	2,473.4
Depreciation charge for the year	4.2	232.4	–	10.3	246.9
Disposals	(3.3)	(32.0)	–	(4.0)	(39.3)
Reclassifications	–	3.5	–	(3.5)	–
Depreciation at 31 March 2006	38.5	2,551.6	–	90.9	2,681.0
Net book value at 31 March 2006	**115.2**	**3,737.2**	**654.6**	**13.3**	**4,520.3**
Net book value at 31 March 2005	118.1	3,520.2	589.0	10.3	4,237.6

The net book value of land and buildings comprised:

	2006 £m	2005 £m
Freehold	**93.0**	93.9
Long leasehold (over 50 years)	**2.7**	2.7
Short leasehold (under 50 years)	**19.5**	21.5
	115.2	118.1

The cost of property, plant and equipment (net of disposals) at 31 March 2006 included £434.4m (2005: £401.7m) relating to interest capitalised.

Included within trade and other payables and other non-current liabilities at 31 March 2006 are contributions to the cost of property, plant and equipment amounting to £3.6m (2005: £19.9m) and £110.8m (2005: £85.1m) respectively.

The carrying value of property, plant and equipment which is carried at deemed cost within plant and machinery at the date of transition to IFRS on 1 April 2004 amounted to £106m.

14. Other non-current receivables

	2006 £m	2005 £m
Lease debtors	**23.3**	31.2
Corporation tax recoverable	**–**	4.2
Other debtors	**0.1**	–
	23.4	35.4

15. Financial instruments

The Group's treasury policy, described in the Directors' report on pages 7 and 8, includes details of the objectives, policies and strategies of the Group associated with financial instruments.

The Group's counterparty exposure under derivative financial contracts at 31 March 2006 was £37.9m (2005: £17.1m).

The Group had no significant exposure to either individual counterparties or geographical groups of counterparties at 31 March 2006.

Book and fair values of financial instruments at 31 March were as follows:

	2006		2005	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Borrowings (excluding bank overdrafts)	**(2,990.5)**	**(3,226.8)**	(3,063.8)	(3,216.4)
Cash and cash equivalents	**23.9**	**23.9**	22.9	22.9
Bank overdrafts	**(15.6)**	**(15.6)**	(18.0)	(18.0)
Financial investments	**–**	**–**	28.0	31.9
Trade and other receivables	**488.1**	**488.1**	570.6	570.6
Trade and other payables	**(709.0)**	**(709.0)**	(801.4)	(801.4)
Other financial liabilities	**(3.9)**	**(3.9)**	(4.9)	(4.9)
Derivative financial assets	**39.2**	**39.2**	–	–
Derivative financial liabilities	**(18.5)**	**(18.5)**	(7.1)	(6.9)

Market values, where available, have been used to determine fair values. Where market values are not available, fair values have been calculated by discounting cash flows at prevailing interest rates. It is assumed that because of short maturities, the fair value of short-term receivables and payables approximates their book value.

Currency and interest rate composition of financial assets and liabilities

The following table sets out the carrying amount, by contractual maturity, of the Group's non-derivative financial instruments that are exposed to interest rate risks before taking into account currency and interest rate swaps.

At 31 March 2006

Fixed rate	**Within 1 year £m**	**1-2 years £m**	**2-3 years £m**	**3-4 years £m**	**4-5 years £m**	**More than 5 years £m**	**Total £m**
Liabilities							
Other bonds							
Sterling	(25.6)	–	–	–	(247.5)	(868.4)	(1,141.5)
EURO	(9.2)	–	(421.0)	–	–	–	(430.2)
Other	(0.1)	–	–	–	–	(90.3)	(90.4)
	(34.9)	–	(421.0)	–	(247.5)	(958.7)	(1,662.1)

Floating rate	**Within 1 year £m**	**1-2 years £m**	**2-3 years £m**	**3-4 years £m**	**4-5 years £m**	**More than 5 years £m**	**Total £m**
Liabilities							
Bank loans							
Sterling	(0.4)	–	–	–	–	(200.0)	(200.4)
Other	(202.4)	–	–	–	–	–	(202.4)
Other bonds							
Sterling	(5.5)	–	–	–	–	(920.1)	(925.6)
Bank overdrafts							
Sterling	(15.6)	–	–	–	–	–	(15.6)
	(223.9)	–	–	–	–	(1,120.1)	(1,344.0)

15. Financial instruments (continued)

Liquidity analysis

The following is an analysis of cash flows payable by National Grid under financial liabilities by remaining contractual maturities at the balance sheet date:

	Due within 1 year			Due between 1 and 2 years		
	Fixed interest £m	Floating interest £m	Repayment £m	Fixed interest £m	Floating interest £m	Repayment £m
Non-derivative financial liabilities						
Other bonds	(112.6)	–	–	(113.5)	–	–
Bank loans	–	(12.1)	(202.1)	–	(9.9)	–
Other interest bearing liabilities	–	–	(163.2)	–	–	–
Other non-interest bearing liabilities	–	–	(511.6)	–	–	(34.2)
	(112.6)	(12.1)	(876.9)	(113.5)	(9.9)	(34.2)
Derivative liabilities (net)						
Cross currency swaps	–	(5.5)	(6.0)	–	–	–
Foreign exchange forward contracts	–	–	0.1	–	–	–
Interest rate swaps	–	(1.6)	–	(0.2)	(0.5)	–
	–	(7.1)	(5.9)	(0.2)	(0.5)	–
Derivative assets (net)						
Cross currency swaps	(6.3)	–	0.1	(7.4)	–	–
Foreign exchange forward contracts	–	–	1.0	–	–	1.2
Interest rate swaps	0.9	–	(0.2)	(0.3)	–	0.1
	(5.4)	–	0.9	(7.7)	–	1.3
Total at 31 March 2006	(118.0)	(19.2)	(881.9)	(121.4)	(10.4)	(32.9)

	Due between 2 and 3 years			Due 3 years and beyond		
	Fixed interest £m	Floating interest £m	Repayment £m	Fixed interest £m	Floating interest £m	Repayment £m
Non-derivative financial liabilities						
Other bonds	(105.0)	–	(427.5)	(1,560.0)	–	(2,066.0)
Bank loans	–	(9.9)	–	–	(36.0)	(200.0)
Other interest bearing liabilities	–	–	–	–	–	–
Other non-interest bearing liabilities	–	–	–	–	–	–
	(105.0)	(9.9)	(427.5)	(1,560.0)	(36.0)	(2,266.0)
Derivative liabilities (net)						
Cross currency swaps	–	–	–	–	–	–
Foreign exchange forward contracts	–	–	0.5	–	–	–
Interest rate swaps	(0.3)	(0.2)	–	–	–	–
	(0.3)	(0.2)	0.5	–	–	–
Derivative assets (net)						
Cross currency swaps	(4.8)	–	12.8	(14.0)	–	(2.0)
Foreign exchange forward contracts	–	–	–	–	–	–
Interest rate swaps	(0.3)	–	–	52.0	–	–
	(5.1)	–	12.8	38.0	–	(2.0)
Total at 31 March 2006	(110.4)	(10.1)	(414.2)	(1,522.0)	(36.0)	(2,268.0)

15. Financial instruments (continued)

Sensitivity analysis at 31 March 2006

Financial instruments affected by market risk include borrowings, deposits and derivative financial instruments. The following analysis, required by IFRS 7, is intended to illustrate the sensitivity to changes in market variables, being principally UK interest rates on the Group's financial instruments.

The analysis also excludes the impact of movements in market variables on the carrying value of pension obligations and provisions.

The sensitivity analysis has been prepared on the basis that the amount of net debt, the ratio of fixed to floating interest rates of the debt and derivatives portfolio, the proportion of financial instruments in foreign currencies are all constant and on the basis of the hedge designations in place at 31 March 2006. As a consequence this sensitivity analysis relates to the position as at 31 March 2006 and is not representative of the year then ended as all of these varied during the course of 2005/06.

The following assumptions were made in calculating the sensitivity analysis:

- the sensitivity to interest rates relates only to derivative financial instruments, as debt and 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 with no sensitivity assumed for RPI-linked debt;
- changes in the carrying value of derivatives from movements in interest rates designated as cash flow hedges are assumed to be recorded fully within equity;
- changes in the carrying value of derivative financial instruments designated as fair value hedges from movements in interest rates have an immaterial effect on the income statement and equity due to compensating adjustments in the carrying value of debt;
- changes in the carrying value of derivative financial instruments not in hedging relationships only affect the income statement;
- all other changes in the carrying value of derivative financial instruments designated as hedges are fully effective with no impact on the income statement;
- debt with a maturity below one year is floating rate for the accrued interest part of the calculation;
- the floating leg of any swap or any floating rate debt is treated as not having any interest rate already set, therefore a change in interest rates affects a full twelve month period for the accrued interest portion of the sensitivity calculations.

Using the above assumptions, the following table shows the illustrative effect on the income statement and equity that would result from movements in changes in UK interest rates.

	Income statement +/- £m	Equity +/- £m
UK interest rates +/- 0.10%	1.4	0.4

Derivative financial instruments

The Group's hedging policies are set out on pages 14 and 15. The Group has entered into a number of derivative financial instruments as detailed below which are designated as follows:

Fair value hedges

The Group maintains interest rate and currency swap contracts as fair value hedges of the interest rate and currency risk on fixed rate debt issued by the Group. Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The gain or loss relating to the effective portion of the interest rate swaps hedging fixed rate borrowings is recognised in the income statement within interest expense and other finance costs. The gain or loss relating to the ineffective portion is recognised in the income statement within net gains/(losses) on derivative financial instruments. Changes in the fair value of the hedged fixed rate borrowings attributable to interest rate risk are recognised in the income statement within interest expense and other finance costs.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount is amortised to the income statement under the effective interest method.

Cash flow hedges

The Group maintains interest rate swaps and cross currency swaps that qualify for hedge accounting as designated cash flow hedges relating to future interest payments on debt. The revaluation of these swaps is included in the cash flow hedge reserve and is recycled to the income statement as the interest charge relating to the debt is recorded.

The Group uses forward foreign currency contracts to hedge anticipated and committed future purchases. Where designated, these contracts qualify for hedge accounting and are designated as cash flow hedges. When the underlying purchase is recorded, the associated gains and losses deferred in equity are removed and included in the initial cost of the asset.

15. Financial instruments (continued)

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derivatives not in a formal hedge relationship

The Group's 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 appropriate.

Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement within net gains/(losses) on derivative financial instruments.

The maturity of derivative financial assets and liabilities measured at fair value at 31 March 2006 can be analysed as follows:

	Maturity less than 1 year £m	Maturity 1-2 years £m	Maturity 2-3 years £m	Maturity 3-4 years £m	Maturity 4-5 years £m	Maturity over 5 years £m	Total fair value 2006 £m
Derivative financial assets							
Interest rate swaps	7.1	–	–	–	–	18.0	25.1
Cross currency swaps	8.5	–	5.5	–	–	–	14.0
Foreign exchange forward contracts	0.1	–	–	–	–	–	0.1
	15.7	–	5.5	–	–	18.0	39.2
Derivative financial liabilities							
Interest rate swaps	(2.3)	–	(0.5)	–	(0.5)	–	(3.3)
Cross currency swaps	(6.2)	–	–	–	–	(9.0)	(15.2)
	(8.5)	–	(0.5)	–	(0.5)	(9.0)	(18.5)
	7.2	**–**	**5.0**	**–**	**(0.5)**	**9.0**	**20.7**

The notional amounts of the above derivatives at 31 March 2006 can be analysed as follows:

	Maturity less than 1 year £m	Maturity 1-2 years £m	Maturity 2-3 years £m	Maturity 3-4 years £m	Maturity 4-5 years £m	Maturity over 5 years £m	Total fair value 2006 £m
Derivative financial assets							
Interest rate swaps	(62.0)	–	–	–	–	(506.0)	(568.0)
Cross currency swaps	–	–	(414.0)	–	–	–	(414.0)
Foreign exchange forward contracts	2.1	–	–	–	–	–	2.1
	(59.9)	–	(414.0)	–	–	(506.0)	(979.9)
Derivative financial liabilities							
Interest rate swaps	(309.0)	–	(80.0)	–	(86.0)	–	(475.0)
Cross currency swaps	(207.0)	–	–	–	–	(100.2)	(307.2)
	(516.0)	–	(80.0)	–	(86.0)	(100.2)	(782.2)
	(575.9)	**–**	**(494.0)**	**–**	**(86.0)**	**(606.2)**	**(1,762.1)**

15. Financial instruments (continued)

At 31 March 2006	Assets Fair value £m	Assets Notional amount £m	Liabilities Fair value £m	Liabilities Notional amount £m
Fair value hedge derivative instruments				
Interest rate swaps	24.7	(506.0)	(0.4)	(71.0)
Cross currency swaps	11.3	(334.0)	(9.0)	(100.2)
	36.0	(840.0)	(9.4)	(171.2)
Cash flow hedge derivative instruments				
Interest rate swaps	-	-	(1.7)	(287.0)
Cross currency swaps	2.7	(80.0)	(6.2)	(207.0)
Foreign exchange forward contracts	0.1	2.1	-	-
	2.8	(77.9)	(7.9)	(494.0)
Other derivative instruments				
Interest rate swaps	0.4	(62.0)	(1.2)	(117.0)
	0.4	(62.0)	(1.2)	(117.0)
Derivative instruments can be analysed as follows:				
Current	15.7	(59.9)	(8.5)	(516.0)
Non-current	23.5	(920.0)	(10.0)	(266.2)
Total	**39.2**	**(979.9)**	**(18.5)**	**(782.2)**

Gains and losses recognised in the cash flow hedge reserve (note 26) on interest rate swap contracts as of 31 March 2006 will be continuously released to the income statement until the borrowings are repaid (note 20).

The amount of cash flow hedge reserve due to be released from reserves to the income statement within the next year is £2.5m, with the remaining amount due to be released with the same maturity profile as borrowings in note 20.

Financial instrument disclosures for the year ended 31 March 2005

The following information for 2005 shows certain of the disclosures required by UK GAAP (FRS 13 'Derivatives and other Financial Instruments: Disclosures').

The notional principal amounts relating to financial instruments held at 31 March 2005 to manage interest rate and currency profiles for interest rate swaps and forward rate agreements; and foreign currency contracts and cross-currency swaps amounted to £1,180m and £622m respectively.

Gains and losses on hedges for the year ended 31 March 2005

	Unrecognised gains £m	Unrecognised losses £m	Unrecognised net gain/(loss) £m	Deferred gains £m	Deferred losses £m	Deferred net gain/(loss) £m
Gains/(losses) on hedges at 1 April 2004	15.4	(20.6)	(5.2)	–	(2.0)	(2.0)
(Gains)/losses arising in previous years recognised in the year	(1.3)	–	(1.3)	–	0.7	0.7
Gains/(losses) arising in previous years not recognised in the year	14.1	(20.6)	(6.5)	–	(1.3)	(1.3)
Gains/(losses) arising in the year	–	6.7	6.7	4.7	(2.7)	2.0
Gains/(losses) on hedges at 31 March 2005	14.1	(13.9)	0.2	4.7	(4.0)	0.7
Of which:						
Gains/(losses) expected to be recognised within one year	0.3	(1.0)	(0.7)	0.9	(1.3)	(0.4)
Gains/(losses) expected to be recognised after one year	13.8	(12.9)	0.9	3.8	(2.7)	1.1

15. Financial instruments (continued)

Currency and interest rate composition of financial assets and liabilities at 31 March 2005

The currency and interest rate composition of the Group's financial assets are shown in the table below after taking into account currency and interest rate swaps:

				Fixed rate assets	
	Total £m	Variable rate £m	Fixed rate £m	Weighted average interest rate %	Weighted average period for which rate is fixed years
At 31 March 2005					
Cash and investments and overdrafts (sterling)	22.9	22.9	–	–	–
Net investment in finance lease (sterling)	38.6	–	38.6	11.5	4.1
	61.5	22.9	38.6	11.5	4.1

In addition to the assets included in the above analysis the Group also held investments in the shares of National Grid plc as detailed in note 16 for the purpose of satisfying obligations under various share option schemes.

Cash and deposits earn interest at prevailing rates for maturity periods not exceeding 12 months.

The currency and interest rate composition of the Group's financial liabilities are shown in the table below after taking into account currency and interest rate swaps:

				Fixed rate liabilities	
	Total £m	Variable rate £m	Fixed rate £m	Weighted average interest rate %	Weighted average period for which rate is fixed years
At 31 March 2005					
Borrowings and overdrafts (sterling)	3,088.9	2,020.1	1,068.8	5.9	10.4
Preference shares of £1 each	43.4	43.4	–	–	–
Other financial liabilities (sterling)	4.9	4.9	–	–	–
	3,137.2	2,068.4	1,068.8	5.9	10.4

The maturity profile of the Group's financial assets and liabilities are shown in the table below after taking into account currency and interest rate swaps:

Maturity of financial assets and liabilities at 31 March 2005

	Assets £m	Liabilities £m
In one year or less	30.1	476.9
In more than one year, but not more than two years	8.1	207.4
In more than two years, but not more than three years	9.0	0.4
In more than three years, but not more than four years	10.0	414.5
In more than four years, but not more than five years	4.3	0.5
In more than five years	–	2,037.5
	61.5	3,137.2

Other financial liabilities relates to an onerous operating lease (see note 22).

Substantially all of the variable rate borrowings and preference shares are subject to interest rates which fluctuate with LIBOR for the appropriate currency at differing premiums.

In calculating the weighted average number of years for which interest rates are fixed, swaps which are cancellable at the option of the swap provider are taken to have a life based on the earliest date at which they can be cancelled.

16. Fixed asset investments

	Listed investments £m
Cost at 1 April 2004	34.6
Additions	0.4
Disposals	(6.8)
Cost at 31 March 2005	28.2
Additions	7.1
Disposals	(35.3)
Cost at 31 March 2006	–
Impairment at 1 April 2004	2.2
Disposals	(2.0)
Impairment at 31 March 2005	0.2
Disposals	(0.2)
Impairment at 31 March 2006	–
Net book value at 31 March 2006	**–**
Net book value at 31 March 2005	28.0

Listed investments at 31 March 2005 related to 6.5m 10p ordinary shares in National Grid plc held by employee share trusts for the purpose of satisfying certain obligations under the various share option schemes. The carrying value at 31 March 2005 of £28.0m (market value £31.9m) represented the cost of these shares less provision for impairment. Funding was provided to the trusts by the Group. The trusts waived their rights to dividends on these shares.

The disposal of fixed asset investments of £35.5m in the year relates to share options exercised by participants in the various Sharesave and share option schemes.

17. Inventories

	2006 £m	2005 £m
Raw materials and consumables	**14.2**	13.6
Work in progress	**1.6**	0.2
	15.8	13.8

The Group consumed £4.1m of inventories during the year (2005: £5.6m).

The above table includes £2.0m of provision for obsolescence as at March 2006 (2005: £2.0m).

18. Trade and other receivables

	2006 £m	2005 £m
Trade debtors	**12.5**	29.0
Amounts owed by other group undertakings	**301.6**	392.1
Other debtors	**11.1**	21.9
Corporation tax recoverable	**11.3**	30.5
Prepayments and accrued income	**142.8**	106.7
	479.3	580.2

Concentrations of credit risk with respect to trade debtors are limited due to the Group's customer base being large and unrelated. Due to this, management believe there is no further credit risk provision required in excess of normal provision for doubtful debts.

Included within trade debtors is the following provision for doubtful debts:

Provision for doubtful debts

	£m
At 1 April 2004	(0.7)
Charge for the year	(0.6)
At 31 March 2005	(1.3)
Released in the year	0.6
At 31 March 2006	**(0.7)**

19. Cash and cash equivalents

	2006 £m	2005 £m
Cash at bank and in hand	**23.9**	22.1
Short-term deposits	**–**	0.8
Cash and cash equivalents	**23.9**	22.9
Bank overdrafts	**(15.6)**	(18.0)
Net cash and cash equivalents	**8.3**	4.9

20. Borrowings

The following table analyses the Group's total borrowings (excluding bank overdrafts):

	2006 £m	2005 £m
Current:		
Bank loans	**202.8**	–
Commercial paper	**–**	207.6
Other bonds	**40.4**	250.8
	243.2	458.4
Non-current:		
Bank loans	**200.0**	407.0
Other bonds	**2,547.3**	2,205.5
	2,747.3	2,612.5
Total borrowings	**2,990.5**	3,070.9

	2006 £m	2005 £m
Total borrowings are repayable as follows:		
In one year or less	**243.2**	458.4
In more than one year, but not more than two years	**–**	207.0
In more than two years, but not more than three years	**421.0**	–
In more than three years, but not more than four years	**–**	414.0
In more than four years, but not more than five years	**247.5**	–
In more than five years		
– by instalments	**–**	–
– other than by instalments	**2,078.8**	1,991.5
	2,990.5	3,070.9

The notional amount outstanding of the Group's debt portfolio (excluding bank overdrafts) at 31 March 2006 was £2,878.5m (2005: £3,063.8m).

The principal items included within Other bonds are listed below. Unless otherwise indicated, these instruments were outstanding at both 31 March 2006 and 31 March 2005.

20. Borrowings (continued)

Issuer	Description of instrument (notional amount)
National Grid Electricity Transmission plc(i)	GBP 240 million 8.0% Fixed Rate Instruments due 2006
National Grid Electricity Transmission plc	EUR 600 million 4.125% Fixed Rate Instruments due 2008
National Grid Electricity Transmission plc	GBP 250 million 4.75% Fixed Rate Instruments due 2010
National Grid Electricity Transmission plc	GBP 300 million 2.983% Guaranteed Retail Price Index-Linked Instruments due 2018
National Grid Electricity Transmission plc	GBP 220 million 3.806% Retail Price Index-Linked Instruments due 2020
National Grid Electricity Transmission plc	GBP 450 million 5.875% Fixed Rate Instruments due 2024
National Grid Electricity Transmission plc	GBP 360 million 6.5% Fixed Rate Instruments due 2028
National Grid Electricity Transmission plc	GBP 70 million 3.589% Limited Retail Price Index-Linked Instruments due 2030
National Grid Electricity Transmission plc	GBP 50 million 2.817% Guaranteed Limited Retail Price Index-Linked Instruments due 2032
National Grid Electricity Transmission plc	GBP 75 million 5.0% Fixed Rate Instruments due 2035
National Grid Electricity Transmission plc (ii)	GBP 50 million 2.2280% Retail Price Index-Linked Instruments due 2035
National Grid Electricity Transmission plc (ii)	GBP 25 million 2.0752% Retail Price Index-Linked Instruments due 2035
National Grid Electricity Transmission plc (ii)	JPY 10 billion 2.81% Fixed Rate Instruments due 2035
National Grid Electricity Transmission plc (ii)	JPY 10 billion 2.755% Fixed Rate Instruments due 2035
National Grid Electricity Transmission plc (ii)	GBP 75 million 2.0353% Retail Price Index-Linked Instruments due 2035
National Grid Electricity Transmission plc (ii)	GBP 25 million 1.9949% Retail Price Index-Linked Instruments due 2035
National Grid Electricity Transmission plc (ii)	GBP 50 million 1.8204% Retail Price Index-Linked Instruments due 2035

(i) Matured during the year ended 31 March 2006
(ii) Issued during the year ended 31 March 2006

Borrowing facilities

At 31 March 2006, the Group had £675m undrawn, committed, credit facilities (2005: £485m). £475m of this was held as back-up to commercial paper. The remaining balance was held for general corporate purposes. £25m of the facilities mature within one year, £200m between one and two years and the remainder after two years.

21. Trade and other payables

	2006 £m	2005 £m
Trade payables	**322.4**	253.2
Amounts owed to ultimate parent company	**17.4**	19.9
Amounts owed to group undertakings	**310.8**	432.4
Social security and other taxes	**25.0**	22.7
Other payables	**24.2**	94.4
Deferred income	**63.8**	63.7
	763.6	886.3

Amounts owed to group undertakings include £43.4m (2005: £43.4m) in respect of 43,406,000 (2005: 43,406,000) preference shares of £1 each held by the parent company. The authorised preference share capital is 74,803,600 (2005: 74,803,600) shares of £1 each. The preference shares, which are non-voting except in matters that directly affect their rights or in the event their dividends are in arrears, are entitled to a dividend of 1% above LIBOR and have a preferential right to a return of capital on a winding-up. The dividend is classified as a finance cost.

22. Provisions

	Environmental £m	Other £m	Total £m
At 1 April 2004	10.3	13.8	24.1
Additions	–	1.8	1.8
Unused amount reversed	(0.5)	–	(0.5)
Utilised	(0.5)	(2.7)	(3.2)
At 31 March 2005	9.3	12.9	22.2
Additions	–	2.4	2.4
Utilised	(1.5)	(3.0)	(4.5)
At 31 March 2006	**7.8**	**12.3**	**20.1**

Provisions have been analysed between current and non-current as follows:

	2006 £m	2005 £m
Current	**2.9**	10.8
Non-current	**17.2**	11.4
	20.1	22.2

The environmental provision relates to estimated liabilities relating to uninsured events, principally of an environmental nature. The assessment of this liability is subject to periodic reviews, which may result in the amount being revised. It is currently estimated that substantially all of this provision will be utilised within the next five years. Other provisions include employer liability provisions of £6.8m (2005: £4.8m) which comprise estimates of liabilities in respect of past events for which no payment date can be identified although it is expected that the liability will be substantially settled over 30 years. Of the remaining balance within other provisions, £3.9m (2005: £4.9m) relates to other property commitments estimated to be utilised over the next nine years and £1.6m (2005: £1.7m) relates to a provision created during the previous year to cover protected rights for employees where NGET has an obligation under several deeds of covenant. Other provisions in 2005 included a severance provision of £1.5m utilised in the year.

The environmental provision is calculated on an undiscounted basis.

23. Other non-current liabilities

	2006 £m	2005 £m
Other payables	**34.2**	1.5
Deferred income	**113.2**	87.7
	147.4	89.2

24. Deferred tax assets and liabilities

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

	Accelerated tax depreciation £m	Employee share options £m	Pensions £m	Cashflow hedge reserve £m	Other net temporary differences £m	Total £m
At 1 April 2004	826.6	(2.1)	(135.8)	–	(6.6)	682.1
Charged/(credited) to income statement	5.4	(1.8)	(4.0)	–	(1.0)	(1.4)
Charged/(credited) to equity	–	(1.0)	13.2	–	–	12.2
At 31 March 2005	832.0	(4.9)	(126.6)	–	(7.6)	692.9
Adoption of IAS 39	–	–	–	(3.3)	–	(3.3)
At 1 April 2005	832.0	(4.9)	(126.6)	(3.3)	(7.6)	689.6
Charged/(credited) to income statement	1.6	(2.0)	(3.2)	–	4.1	0.5
Charged/(credited) to equity	–	(2.7)	12.7	(0.1)	–	9.9
At 31 March 2006	**833.6**	**(9.6)**	**(117.1)**	**(3.4)**	**(3.5)**	**700.0**

All of the deferred tax assets were available for offset against deferred tax liabilities and hence the net deferred tax provision at 31 March 2006 was £700.0m (2005: £692.9m). At the balance sheet date there were no material current deferred tax assets or liabilities.

No asset has been recognised for capital losses carried forward. These losses are available to reduce future capital gains. The benefit will only arise if assets giving rise to a capital gain are sold in future periods. The unrecognised deferred tax asset is £1.7m (2005: £1.7m).

There are no other unrecognised deferred tax assets or liabilities.

25. Share capital

	Allotted, called up and fully paid	
	number	£m
At 1 April 2004	31,870	–
Issued during the year	3,187,000	334.9
Capital reduction	–	(334.6)
At 31 March 2005	3,218,870	0.3
Movement during the year	–	–
At 31 March 2006	**3,218,870**	**0.3**

There has been no movement in share capital during the year. The movement in share capital for the year ended 31 March 2005 is explained in note 26.

At 31 March 2006 the authorised ordinary share capital of the Group was £200.3m (2005: £200.3m) relating to 2,003,155,130 (2005: 2,003,155,130) ordinary shares of 10 pence each.

Share option and award schemes

National Grid plc operates two principal forms of share option scheme in which the employees and Directors of the Group are entitled to participate. They are an employee Sharesave scheme and an Executive Share Option Plan ('the Executive Plan'). The details given below relate to the schemes operated by National Grid plc for the benefit of the Group's employees and Directors.

The Sharesave scheme is savings related where, under normal circumstances, share options are exercisable on completion of a three or a five year save-as-you-earn contract. The exercise price of options granted represents 80% of the market price at the date the option was granted.

The Executive Plan applies to senior executives, including Executive Directors. Options granted for the 1999/2000 financial year are subject to the achievement of performance targets related to earnings per share growth over a three year period and have now vested. Options granted for the 2000/01 financial year and thereafter are subject to the achievement of performance targets related to total shareholder returns over a three year period. The share options are generally exercisable between the third and tenth anniversaries of the date of grant if the relevant performance target is achieved.

National Grid plc also operates a number of share award schemes including a Performance Share Plan (PSP) and a Share Matching Plan.

Under the PSP awards have been made to Executive Directors and a number of senior staff below the level of the Executive Management Team who have significant influence over the Group's ability to meet its strategic objectives. Under the PSP, awards are conditional on the Group's total shareholder return over a three year period. Awards are delivered in National Grid plc ordinary shares. At 31 March 2006 the number of conditional awards of ordinary share equivalents outstanding under the PSP was 3,351,044 (2005: 2,288,973) of which nil (2005: nil) were exercisable. The number of conditional awards during the year ended 31 March 2006 was 1,080,244 (2005: 1,208,541) with awards transferred to the Group during the year of 35,782 (2005: nil), lapses/forfeits of 53,955 (2005: 45,179) and exercises of nil (2005: nil).

The Share Matching Plan applies to Executive Directors whereby a predetermined part of each Director's bonus entitlement is automatically deferred into National Grid plc shares and a matching award may be made under the Plan after a three year period provided the Director is still employed by the Group. At 31 March 2006 the number of conditional awards on ordinary share equivalents outstanding under the Share Matching Plan was 317,618 (2005: 262,576) of which 44,339 (2005: 21,088) were exercisable. The number of conditional awards during the year ended 31 March 2006 was 87,877 (2005: 107,614) with awards transferred to the Group during the year of 5,730 (2005: nil) and exercises of 38,565 (2005: 40,117).

25. Share capital (continued)

Share option and award schemes (continued)

Movements in options to subscribe for ordinary shares under the Group's various option schemes for the two years ended 31 March 2006 are shown below and include those options related to shares issued to employee benefit trusts:

	Sharesave scheme options		Executive options		Total options
	Weighted average price £ per share	millions	Weighted average price £ per share	millions	millions
At 1 April 2004	3.46	6.1	4.70	4.8	10.9
Granted	3.83	1.2	–	–	1.2
Lapsed – expired	3.76	(0.3)	5.20	(0.2)	(0.5)
Exercised	3.42	(1.3)	3.67	(0.4)	(1.7)
At 31 March 2005	3.54	5.7	4.77	4.2	9.9
Staff transferred	–	–	3.88	1.0	1.0
Granted	4.34	1.0	–	–	1.0
Lapsed – expired	4.01	(0.3)	5.16	(0.4)	(0.7)
Exercised	3.78	(0.8)	3.91	(1.4)	(2.2)
At 31 March 2006	**3.63**	**5.6**	**4.81**	**3.4**	**9.0**

Included within options outstanding at 31 March 2006 and 31 March 2005 were the following options which were exercisable:

At 31 March 2006	**3.50**	**0.1**	**4.84**	**3.3**	**3.4**
At 31 March 2005	4.52	0.1	4.82	2.7	2.8

The weighted average remaining contractual life of options in the employee Sharesave scheme at 31 March 2006 was 2 years and 7 months. These options have exercise prices between £3.17 and £4.57.

The weighted average share price at the exercise dates were as follows:

	2006 £ per share	2005 £ per share
Sharesave scheme options	**5.64**	4.28
Executive Plan options	**5.41**	4.65

Options outstanding and exercisable and their weighted average exercise prices for the respective ranges of exercise prices and years at 31 March 2006 are as follows:

	Weighted average exercise price of exercisable options £ per share	Number exercisable millions	Weighted average exercise price of outstanding options £ per share	Number outstanding millions	Exercise price per share pence	Normal dates of exercise years
Executive plan	2.81	0.2	2.81	0.2	280.5	2001 – 2008
	3.83	0.2	3.83	0.2	375.8 – 490.0	2002 – 2009
	4.41	0.1	4.41	0.1	435.8 – 455.3	2003 – 2010
	5.28	0.8	5.28	0.8	526.0 – 531.5	2004 – 2011
	5.37	1.1	5.37	1.1	479.5 – 563.0	2005 – 2012
	4.72	0.9	4.72	0.9	460.3 – 481.5	2006 – 2013
	–	–	4.05	0.1	405.0	2007 – 2014
	4.84	**3.3**	**4.81**	**3.4**		

Share-based payment charges

Under International Financial Reporting Standards, a charge is made to the income statement based on the fair value of grants in accordance with IFRS 2 'Share-based Payment'. All share awards are equity settled.

The charge to the income statement for the year ended 31 March 2006 was £2.2m (2005: £4.0m).

25. Share capital (continued)

Awards under share option plans

The average share prices at the date of options being granted during each of the two financial years ended 31 March were as follows:

	2006	2005
Where the exercise price is less than the market price at the date of the grant	**569.0p**	496.0p

The average exercise prices of the options granted during each of the two financial years ended 31 March were as follows:

	2006	2005
Where the exercise price is less than the market price at the date of the grant	**434.0p**	182.9p

The average fair values of the options granted during each of the two financial years ended 31 March were estimated as follows:

	2006	2005
Where the exercise price is less than the market price at the date of the grant	**127.8p**	145.6p

The fair value of the options granted were estimated using the following principal assumptions:

	2006	2005
Dividend yield (%)	**4.5**	5.3 – 5.8
Volatility (%)	**15.6 – 18.9**	15.4
Risk-free investment rate (%)	**4.2**	4.5
Average life (years)	**4.2**	4.1

The fair values of awards under the Sharesave scheme have been calculated using the Black-Scholes model. This is considered appropriate given the short exercise window of sharesave options.

Volatility has been derived based on the following:

(i) implied volatility in traded options over National Grid plc's traded shares;

(ii) historical volatility of National Grid plc's shares from October 2002 (the date of the merger of National Grid Group plc and Lattice Group plc); and

(iii) implied volatility of comparator companies where options in their shares are traded.

Volatility is assumed to revert from its current implied level to its long run mean, based on historical volatility under (ii) above.

Awards under other share scheme plans

The average share prices and fair values at the date share awards were granted during each of the two financial years ended 31 March were as follows:

	2006	2005
Average share price	**535.5p**	423.9p
Average fair value	**360.7p**	198.9p

The fair values of the awards granted were estimated using the following principal assumptions:

	2006	2005
Dividend yield (%)	**4.4**	5.3 – 5.7
Volatility (%)	**15.6**	15.4
Risk-free investment rate (%)	**4.1**	4.5 – 5.2

The fair values have been calculated using a Monte Carlo simulation model, which better reflects the total shareholder return performance conditions of the plan.

For other share scheme awards, where the primary vesting condition is that employees complete a specified number of years service, the fair value has been calculated as the share price at date of grant, adjusted to recognise the extent to which participants do not receive dividends over the vesting period.

Volatility for share awards has been calculated on the same basis as used for share options, as described above.

26. Reconciliation of movements in total equity

	Called-up ordinary share capital £m	Share premium account £m	Capital redemption reserve £m	Special reserve £m	Cash flow hedge reserve £m	Retained earnings £m	Total £m
At 1 April 2004	–	454.1	0.1	28.8	–	386.5	869.5
Net income recognised directly in equity	–	–	–	–	–	31.7	31.7
Profit for the year	–	–	–	–	–	361.7	361.7
Equity dividends paid	–	–	–	–	–	(1,450.0)	(1,450.0)
Bonus issue of shares	334.9	–	–	(28.8)	–	(306.1)	–
Capital reduction	(334.6)	(454.1)	–	–	–	788.7	–
At 31 March 2005	0.3	–	0.1	–	–	(187.5)	(187.1)
Adoption of IAS 39	–	–	–	–	(7.5)	3.8	(3.7)
At 1 April 2005	0.3	–	0.1	–	(7.5)	(183.7)	(190.8)
Net income/(expense) recognised directly in equity	–	–	–	–	(0.4)	30.8	30.4
Profit for the year	–	–	–	–	–	292.4	292.4
At 31 March 2006	**0.3**	**–**	**0.1**	**–**	**(7.9)**	**139.5**	**132.0**

The Group has no non-distributable reserves (2005: £nil; 2004: £334.9m).

On 24 March 2005, the Group issued 3,187,000 ordinary shares of £105.08 each at nominal value by way of a bonus issue through the capitalisation of non-distributable reserves, being the special reserve and the non-distributable element of retained earnings amounting to £334.9m which was credited to share capital. The Group then underwent a Court-approved capital reduction scheme, reducing the nominal value of these shares to 10 pence each, thereby reducing share capital by £334.6m, and also reducing the share premium account to zero. The net result of these transactions was to increase distributable reserves by £788.7m and share capital by £0.3m (see note 25) as compared with the position immediately prior to the issue of shares on 24 March 2005.

27. Group cash flow statement

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

	2006 £m	2005 £m
Movement in cash and cash equivalents	**3.4**	(1.8)
Decrease/(increase) in borrowings and derivatives	**148.5**	(240.5)
Net interest paid (i)	**144.3**	–
Change in net debt resulting from cash flows	**296.2**	(242.3)
Net interest charge (i)	**(161.8)**	–
Other non-cash movements	**(5.0)**	(21.3)
Movement in net debt (net of related derivative financial instruments) in the year	**129.4**	(263.6)
Net debt at the start of the year	**(3,066.0)**	(2,802.4)
Impact of adoption of IAS 32 and IAS 39 (i)	**(24.9)**	–
Net debt (net of related derivative financial instruments) at the end of the year	**(2,961.5)**	(3,066.0)

(i) The adoption of IAS 39 resulted in changes to the carrying value of borrowings as at 1 April 2005 as described in note 2.

b) Analysis of changes in net debt

	At 1 April 2004 £m	Cash flow £m	Interest accretion £m	At 31 March 2005 £m
Cash and cash equivalents	27.1	(4.2)	–	22.9
Bank overdrafts	(20.4)	2.4	–	(18.0)
Borrowings due within one year excluding bank overdrafts	–	(458.4)	–	(458.4)
Borrowings due after one year	(2,809.1)	217.9	(21.3)	(2,612.5)
	(2,802.4)	**(242.3)**	**(21.3)**	**(3,066.0)**

	At 1 April 2005 £m	Impact of adoption of IAS 32 and IAS 39 (i) £m	Cash flow £m	Other non-cash movements £m	At 31 March 2006 £m
Cash and cash equivalents	22.9	–	1.0	–	23.9
Bank overdrafts	(18.0)	–	2.4	–	(15.6)
Borrowings due within one year excluding bank overdrafts	(458.4)	(38.4)	256.3	(2.7)	(243.2)
Borrowings due after one year	(2,612.5)	11.1	(107.8)	(38.1)	(2,747.3)
Derivative financial assets	–	2.4	–	36.8	39.2
Derivative financial liabilities	–	–	–	(18.5)	(18.5)
	(3,066.0)	**(24.9)**	**151.9**	**(22.5)**	**(2,961.5)**

(i) There are no comparatives for net debt related derivative assets and liabilities as the Group adopted IAS 39 with effect from 1 April 2005 consistent with the requirements of IFRS 1. The adoption of IAS 39 also resulted in changes to the carrying value of borrowings as at 1 April 2005 (see note 2).

28. Commitments and contingencies

a) Future capital expenditure

	2006 £m	2005 £m
Contracted for but not provided	**336.5**	220.7

b) Lease commitments

At 31 March 2006, the Group's operating lease commitments, which relate to land and buildings, for the financial year ending 31 March 2007 amounted to £2.9m (2005: £4.2m) with lease expiry dates all falling due after five years.

Total Group commitments under non-cancellable operating leases were as follows:

	2006 £m	2005 £m
In one year or less	**2.9**	4.2
In more than one year, but not more than two years	**2.9**	4.2
In more than two years, but not more than three years	**2.9**	4.2
In more than three years, but not more than four years	**2.9**	4.2
In more than four years, but not more than five years	**2.9**	4.2
In more than five years	**12.8**	22.9
	27.3	43.9

The total of future minimum sublease payments expected to be received under non-cancellable subleases is £5.0m (2005: £5.2m).

c) Guarantees and performance bonds

The Company has issued performance bonds in the ordinary course of business amounting to £5.3m (2005: £6.9m) and guarantees in respect of the performance of a third party up to £14.0m (2005: £14.0m).

29. Related party transactions

Transactions with related parties were in the normal course of business and are summarised below:

	2006 £m	2005 £m
Sales:		
Services supplied to group undertakings	**0.8**	2.0
Purchases:		
Services received from group undertakings	**14.6**	15.0

It is not practical to identify the intercompany trading transactions for all related parties because the intercompany balances are transferred to an intercompany loan with National Grid Holdings One plc, the parent of the Company's immediate parent company, on a monthly basis. This is as a result of new transfer pricing rules which require that intercompany transactions must be accounted for on an arms length financing basis.

At 31 March 2006, the Group had amounts receivable and payable amounting to £301.6m (2005: £392.1m) and £328.2m (2005: £452.3m) respectively with group undertakings and had amounts payable to pension funds amounting to £1.7m (2005: £1.8m). Employer contributions made to the Electricity Supply Pension Scheme are set out in note 8.

The Company has been given a guarantee by National Grid Holdings One plc for £23 million in respect of costs to be incurred in relation to the UK Netherlands interconnector planned to be constructed by BritNed, which is a joint venture owned by National Grid plc and TenneT. This guarantee is unlikely to be called, hence no provision is required.

30. Group undertakings

The principal Group undertaking included in the Group accounts, the issued share capital of which is held by the Company, is NGC Leasing Limited. This undertaking, whose principal activity is that of a leasing company, is wholly-owned and is incorporated in Great Britain. Apart from NGC Leasing, the only other Group undertakings (both wholly owned and incorporated in Great Britain) are NGC Employee Shares Trustee Limited (dormant sharesave trustee company) and Elexon Limited, which the Company holds in a purely nominal capacity and over which it exercises no control.

31. Holding company

The Company's ultimate controlling and parent company is National Grid plc, which owns 100% of the Company's ordinary share capital. The immediate holding company for which consolidated financial statements are prepared is National Grid Holdings Limited. Both companies are incorporated in Great Britain. Copies of their consolidated financial statements can be obtained from their Company Secretary at National Grid plc, 1-3 Strand, London, WC2N 5EH

Independent auditors' report to the members of National Grid Electricity Transmission plc

We have audited the parent company's accounts of National Grid Electricity Transmission plc for the year ended 31 March 2006 which comprise the balance sheet, and the related notes. These accounts have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the accounts in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, 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.

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report, and consider whether it is consistent with the audited accounts. This other information comprises only the Directors' Report and the Business Review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion

In our opinion:

- the accounts give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 March 2006;
- the accounts have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the accounts.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Birmingham
16 May 2006

Notes:

(a) The maintenance and integrity of the National Grid Electricity Transmission plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the accounts since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of accounts may differ from legislation in other jurisdictions.

Company Accounting Policies

for the year ended 31 March 2006

(a) Basis of preparation of accounts
These parent company accounts have been prepared in accordance with the Companies Act 1985 and applicable UK accounting and financial reporting standards.

The accounts have been prepared on an historical cost basis, except for the revaluation of financial instruments from 1 April 2005 onwards.

The preparation of accounts requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

The Company has adopted FRS 21 'Events after the Balance Sheet Date', FRS 23 'The Effects of Changes in Foreign Exchange Rates', FRS 25 'Financial Instruments: Disclosure and Presentation', FRS 26 'Financial Instruments: Measurement' and FRS 29 'Financial Instruments: Disclosure'. The Company has also adopted FRS 17 'Retirement Benefits' in full; previously the Company disclosed the effect of FRS 17 in a note. The impact of the adoption of these standards is shown in note 1.

The Company has not presented its own profit and loss account as permitted by section 230 of the Companies Act 1985.

Changes in accounting policies
The accounting policies are consistent with those of the previous financial year except that the Company has adopted the following standards for which the principal effects of this decision are discussed in note 1:

FRS 23 'The Effects of Changes in Foreign Exchange Rates'

FRS 25 'Financial Instruments: Disclosure and Presentation'

FRS 26 'Financial Instruments: Measurement'

FRS 29 'Financial Instruments: Disclosure'.

(b) Tangible fixed assets and depreciation
Tangible fixed assets are included in the balance sheet at their cost less accumulated depreciation. Cost includes payroll and finance costs incurred which are directly attributable to the construction of tangible fixed assets.

No depreciation is provided on freehold land and assets in the course of construction. Other tangible fixed assets are depreciated, principally 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, which are reviewed on a regular basis, consideration is given to any contractual arrangements and operational requirements. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of tangible fixed assets are as follows:

Depreciation periods for category of assets	Years
Plant and Machinery	
Transmission plant	
– Towers	40 or 60
– Substation plant, overhead lines and cables	40 or 50
– Overhead line spacers	20
– Protection, control and communication equipment	15 or 25
Cross-Channel link	15 to 60
Freehold and leasehold properties	up to 40
Motor vehicles and office equipment	3 or 5

(c) Fixed asset investments
Investments held as fixed assets are stated at cost less any provisions for impairment. 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 net realisable value and its value in use.

(d) Deferred taxation
Deferred taxation is provided in full on all material timing differences, with certain exceptions. No provision is made for any timing differences on non-monetary assets arising from fair value adjustments, except where there is a binding agreement to sell the assets concerned. No provision is made where it is more likely than not that any taxable gain will be rolled over into replacement assets.

Deferred tax assets are only recognised to the extent that they are considered recoverable.

Deferred tax balances have not been discounted.

(e) Stocks
Stocks, which primarily comprise consumable stores and strategic spares, are stated at cost less provision for obsolescence.

(f) Turnover
Turnover primarily represents the sales value derived from the transmission of electricity and the provision of related services. It excludes intra-Group and inter-company transactions and is stated net of value added tax.

Where revenues received or receivable exceed the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, no liability is recognised. Similarly no asset is recognised when a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

(g) Pensions
Following the adoption of FRS 17, the regular service cost of providing retirement benefits to employees during the period, together with the cost of any benefits relating to past service is charged to operating profit in the period.

The interest cost on retirement benefit scheme liabilities less the expected return on the assets of the schemes during the period, based on the market value of the schemes at the start of the period, is charged as other finance charges to profit before taxation in the period.

The difference between the market value of assets and the actuarial value of pension liabilities is shown as a liability in the balance sheet net of deferred tax.

Differences between actual and expected returns on assets and experience gains/(losses) arising on scheme liabilities during the period, together with differences arising from changes in assumptions, are recognised as gains and losses within profit and loss account reserve.

(h) Leases
Finance lease income is allocated to accounting periods so as to give a constant rate of return on the net investment in the lease. The net investment in the finance lease is included in debtors and represents the total rentals receivable, net of finance charges, relating to future periods.

Operating lease payments are charged to the profit and loss account on a straight line basis over the term of the lease.

(i) Financial Instruments
Financial assets, liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities and is recorded at the proceeds received, net of direct issue costs.

Trade debtors do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts. Trade creditors are not interest bearing and are stated at their nominal value.

Loans receivable and other receivables are carried 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 profit and loss account.

Other financial investments are initially measured at cost including transaction costs, but with effect from 1 April 2005 are subsequently carried at fair value. Changes in the fair value of investments classified at fair value through profit and loss are included in the profit and loss statement, while changes in the fair value of investments classified as available for sale are recognised directly in equity, until the investment is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the net profit or loss for the period.

Interest-bearing loans and overdrafts are recorded as the proceeds received, net of direct issue costs plus accrued interest less any repayments. Prior to 1 April 2005 accrued interest is presented as part of current liabilities and not combined with the principal amounts payable.

Derivative financial instruments are recognised initially at fair value, and are subsequently also measured at fair value. Changes in the fair value of derivative financial instruments are included in the profit and loss statement to the extent hedge accounting is not applied.

Subsequent to initial recognition, the fair values of financial instruments measured at fair value that are quoted in active markets are based on bid prices for assets held and offer prices for issued liabilities. When independent prices are not available, fair values are determined by using valuation techniques which refer to observable market data. These include comparison with similar instruments where market observable prices exist, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis using the effective interest rate method.

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets (being assets that necessarily take a substantial period of time to get ready for their intended use or sale) are added to their cost. Such additions cease when the assets are substantially ready for their intended use or sale. All other borrowing costs are recognised in the profit and loss statement in the period in which they are incurred.

(j) Hedge accounting and derivative financial instruments
The Company enters into both derivative financial instruments ('derivatives') and non-derivative financial instruments in order to manage its interest rate and foreign currency exposures. The principal derivatives used include interest rate swaps, forward rate agreements, currency swaps, forward foreign currency contracts and interest rate swaptions.

All derivative transactions are undertaken, or maintained, with a view to providing a commercial hedge of the interest or currency risks associated with the Company's underlying business activities and the financing of those activities.

With effect from 1 April 2005, derivatives are carried in the balance sheet at their fair value.

From 1 April 2005, the accounting policy for hedge accounting is as described below. Disclosures on the impact of implementing FRS 26 at 1 April 2005 are set out in note 1.

Changes in the carrying value of financial instruments that are designated and effective as hedges of future cash flows ('cash flow hedges') are recognised directly in equity and any ineffective portion is recognised immediately in the profit and loss account. Amounts deferred in equity in respect of cash flow hedges are subsequently recognised in the profit and loss account in the same period in which the hedged item affects net profit or loss. Where a non-financial asset or a non-financial liability results from a forecasted transaction or a firm commitment being hedged, the amounts deferred in equity are included in the initial measurement of that non-monetary asset or liability.

Changes in the carrying value of financial instruments that are designated as hedges of the changes in the fair value of assets or liabilities ('fair value hedges') are recognised in the profit and loss account. An equal and opposite amount is recorded as an adjustment to the carrying value of hedged items, with a corresponding entry in the profit and loss account, to the extent that the change is attributable to the risk being hedged and that the fair value hedge is effective.

Changes in the fair value of derivatives that do not qualify for hedge accounting are recognised in the profit and loss account as they arise, within finance costs.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, or 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 profit and loss account in the same periods in which the previously hedged item affects net profit or loss. For fair value hedges the cumulative adjustment recorded to its carrying value at the date hedge accounting is discontinued is amortised to the profit and loss account using the effective interest method.

If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the profit and loss account immediately.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those host contracts and the host contracts are not carried at fair value with unrealised gains or losses reported in the profit and loss account.

Prior to 1 April 2005, derivatives used for hedging purposes were not recorded on the balance sheet as assets or liabilities. Monetary assets and liabilities in foreign currencies were retranslated at hedged rates instead of closing rates.

As permitted by the transition provisions of FRS 26, prior year adjustments have not been made to the balance sheet as at 31 March 2005 or the profit and loss account for the year then ended to reflect the adoption of FRS 26.

(k) Employee benefit trusts
Shares held by employee benefit trusts are carried at cost less provision for impairment. Impairment is measured by reference to the option price of those shares required to settle outstanding options, and by reference to market price, if applicable, for the remainder.

(l) Share-based payments
The Company's ultimate parent company, National Grid plc, 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. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the ultimate parent company's estimate of shares that will eventually vest.

(m) Research and development
Research and development expenditure is charged to the profit and loss account in the period in which it is incurred.

(n) Environmental costs
Provision is made for environmental costs, based on future estimated expenditures, but there is no discounting of any provision to present values.

(o) 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.

Company Balance Sheet

at 31 March

	Notes	2006 £m	2005 (restated)(i) £m
Fixed assets			
Tangible assets	2	**4,592.2**	4,328.9
Derivative financial assets		**23.5**	–
Investments	3	**0.1**	28.1
		4,615.8	4,357.0
Current assets			
Stocks	4	**15.8**	13.8
Debtors	5	**514.0**	636.5
Derivative financial assets		**15.7**	–
Current asset investments		**–**	0.7
Cash at bank and in hand		**21.8**	19.5
		567.3	670.5
Creditors (amounts falling due within one year)			
Borrowings		**(258.8)**	(476.4)
Derivative financial liabilities		**(8.5)**	–
Other creditors		**(761.1)**	(840.3)
	6	**(1,028.4)**	(1,316.7)
Net current liabilities		**(461.1)**	(646.2)
Total assets less current liabilities		**4,154.7**	3,710.8
Creditors (amounts falling due after one year)			
Borrowings		**(2,747.3)**	(2,612.5)
Derivative financial liabilities		**(10.0)**	–
Other creditors		**(147.4)**	(89.2)
	7	**(2,904.7)**	(2,701.7)
Provisions for liabilities and charges			
Deferred tax liabilities		**(819.7)**	(824.5)
Other provisions		**(20.1)**	(22.2)
	9	**(839.8)**	(846.7)
Net assets before post-retirement liability		**410.2**	162.4
Net post-retirement liability	10	**(253.4)**	(279.1)
Net assets/(liabilities)		**156.8**	(116.7)
Capital and reserves			
Called up share capital	11	**0.3**	43.7
Share premium account	12	**–**	–
Capital redemption reserve	12	**0.1**	0.1
Special reserve	12	**–**	–
Cash flow hedge reserve	12	**(7.9)**	–
Profit and loss account	12	**164.3**	(160.5)
Equity shareholders' funds		**156.8**	(160.1)
Non-equity shareholders' funds		**–**	43.4
Total shareholders' funds	12	**156.8**	(116.7)

(i) During the year ended 31 March 2006, the Company adopted FRS 17 'Retirement Benefits', replacing SSAP 24 'Accounting for Pension Costs', in full and comparative figures for 2005 have been restated accordingly.

The notes on pages 51 to 60 form part of the Accounts which were approved by the Board of Directors on 16 May 2006 and were signed on its behalf by:

Nick Winser Director

Andy Chapman Director

Notes to the Company Accounts

1. Changes in accounting policies

During the year, the Company has adopted FRS 17 'Retirement Benefits' in full; previously the Company disclosed the effect of FRS 17 in a note. The Company has also adopted FRS 21 'Events after the Balance Sheet Date', FRS 23 'The Effects of Changes in Foreign Exchange Rates', FRS 25 'Financial Instruments: Disclosure and Presentation', FRS 26 'Financial Instruments: Measurement' and FRS 29 'Financial Instruments: Disclosures'.

FRS 17 'Retirement Benefits'

The Company has adopted FRS 17 'Retirement Benefits', replacing SSAP 24 'Accounting for Pension Costs', in full for the year ended 31 March 2006 and comparative figures for 2005 have been restated accordingly. Disclosures showing the impact on the Company's profit and loss account and balance sheet, together with other disclosures required by FRS 17, are set out in notes 10 and 12. The effect on the net assets at 31 March 2004 and on the profit and loss account for the year ended 31 March 2005 is shown in note 12.

FRS 21 'Events after the Balance Sheet Date'

The adoption of FRS 21 results in a change to the timing of the Company's proposed final dividend if not approved by the balance sheet date. This does not affect the net assets as at 31 March 2005. The effect on the net assets at 31 March 2004 and on the profit and loss account for the year ended 31 March 2005 is shown in note 12.

FRS 23 'The Effects of Changes in Foreign Exchange Rates'
FRS 25 'Financial Instruments: Disclosure and Presentation'
FRS 26 'Financial Instruments: Measurement'
FRS 29 'Financial Instruments: Disclosures'.

The adoption of FRS 23, FRS 25, FRS 26 and FRS 29 has resulted in a change to the accounting for the Company's financial instruments. Derivative financial instruments and available for sale investments are recorded in the balance sheet at fair value, whilst deferred gains and losses relating to items qualifying for hedge accounting are derecognised and instead recorded in equity (for cash flow hedges) or by adjusting the carrying value of the hedged financial instrument (for fair value hedges). Preference shares are recorded as amounts owed to group undertakings instead of as share capital. As permitted by the transition provisions of FRS 26, prior year adjustments have not been made to the balance sheet at 31 March 2005 or the profit and loss account for the year then ended.

The adoption of FRS 23, FRS 25, FRS 26 and FRS 29 reduced net assets at 1 April 2005 by £47.1 million, as shown below:

	£m
Borrowings	(27.3)
Derivative financial assets	2.4
Accrued interest	27.9
Deferred gains and losses	(10.0)
Deferred taxation	3.3
Amounts owed to group undertakings	(43.4)
	(47.1)

It is not practical to calculate the impact of the adoption of FRS 23, FRS 25, FRS 26 and FRS 29 on the results for the year ended 31 March 2006.

2. Tangible fixed 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 2005	155.7	5,878.2	623.3	176.1	6,833.3
Capital expenditure	1.0	2.3	522.8	4.4	530.5
Disposals	(3.3)	(32.0)	–	(2.0)	(37.3)
Reclassifications	0.3	450.7	(488.4)	37.4	–
Cost at 31 March 2006	153.7	6,299.2	657.7	215.9	7,326.5
Depreciation at 1 April 2005	37.6	2,351.9	–	114.9	2,504.4
Charge for the year	4.2	232.9	–	30.1	267.2
Disposals	(3.3)	(32.0)	–	(2.0)	(37.3)
Reclassifications	–	3.9	–	(3.9)	–
Depreciation at 31 March 2006	38.5	2,556.7	–	139.1	2,734.3
Net book value at 31 March 2006	**115.2**	**3,742.5**	**657.7**	**76.8**	**4,592.2**
Net book value at 31 March 2005	118.1	3,526.3	623.3	61.2	4,328.9

The cost of tangible fixed assets (net of disposals) at 31 March 2006 includes £434.4m (2005: £401.7m) relating to interest capitalised.

The net book value of land and buildings comprised:

	2006 £m	2005 £m
Freehold	**93.0**	93.9
Long leasehold (over 50 years)	**2.7**	2.7
Short leasehold (under 50 years)	**19.5**	21.5
	115.2	118.1

3. Fixed asset investments

	Group undertakings £m	Listed investments £m	Total £m
Cost at 1 April 2005	0.1	28.2	28.3
Additions	–	7.1	7.1
Disposals	–	(35.3)	(35.3)
Cost at 31 March 2006	0.1	–	0.1
Impairment at 1 April 2005	–	0.2	0.2
Disposals	–	(0.2)	(0.2)
Impairment at 31 March 2006	–	–	–
Net book value at 31 March 2006	**0.1**	**–**	**0.1**
Net book value at 31 March 2005	0.1	28.0	28.1

Listed investments at 31 March 2005 related to 6.5m 10p ordinary shares in National Grid plc held by employee share trusts for the purpose of satisfying certain obligations under the various share option schemes. The carrying value at 31 March 2005 of £28.0m (market value £31.9m) represented the cost of these shares less provision for impairment. Funding was provided to the trusts by the Company. The trusts waived their rights to dividends on these shares.

Group subsidiary undertakings

Investments in Group undertakings represent ordinary shares at cost. The principal Group undertaking included in the Group accounts, the issued share capital of which is held by the Company, is NGC Leasing Limited. This undertaking, whose principal activity is that of a leasing company, is wholly-owned and is incorporated in Great Britain.

Apart from NGC Leasing, the only other Group undertakings (both wholly owned and incorporated in Great Britain) are NGC Employee Shares Trustee Limited (dormant sharesave trustee company) and Elexon Limited, which the Company holds in a purely nominal capacity and over which it exercises no control.

4. Stocks

	2006 £m	2005 £m
Raw materials and consumables	**14.2**	13.6
Work in progress	**1.6**	0.2
	15.8	13.8

5. Debtors

	2006 £m	2005 £m
Amounts falling due within one year:		
Trade debtors	**12.5**	29.0
Amounts owed by other group undertakings	**304.5**	397.7
Other debtors	**17.5**	28.0
Corporation tax recoverable	**11.3**	30.5
Prepayments and accrued income	**143.8**	107.7
	489.6	592.9
Amounts falling due after more than one year:		
Other debtors	**24.4**	39.4
Corporation tax recoverable	**–**	4.2
	514.0	636.5

6. Creditors (amounts falling due within one year)

	2006 £m	2005 £m
Borrowings (note 8)	**258.8**	476.4
Derivative liabilities	**8.5**	–
Trade creditors and accruals	**322.1**	252.9
Deferred income	**63.8**	63.7
Amounts owed to ultimate parent company	**17.4**	19.9
Amounts owed to group undertakings	**310.1**	386.6
Corporation tax	**–**	–
Social security and other taxes	**24.8**	22.7
Dividends	**–**	1.9
Other creditors	**22.9**	92.6
	1,028.4	1,316.7

Following the adoption of FRS 25 'Financial Instruments: Disclosure and Presentation' at 1 April 2005, amounts owed to group undertakings at 31 March 2006 include £43.4m in respect of 43,406,000 preference shares of £1 each held by the parent company. The authorised preference share capital at 31 March 2006 is 74,803,600 shares of £1 each. The preference shares, which are non-voting except in matters that directly affect their rights or in the event their dividends are in arrears, are entitled to a dividend of 1% above LIBOR and have a preferential right to a return of capital on a winding-up. The dividend is now classified as a finance cost. As permitted by FRS 25, comparative figures at 31 March 2005 have not been restated.

7. Creditors (amounts falling due after more than one year)

	2006 £m	2005 £m
Borrowings (note 8)	**2,747.3**	2,612.5
Derivative liabilities	**10.0**	–
Deferred income	**113.2**	87.7
Other creditors	**34.2**	1.5
	2,904.7	2,701.7

8. Borrowings

	2006 £m	2005 £m
Amounts falling due within one year:		
Bank loans and overdrafts	**218.4**	18.0
Commercial paper	**–**	207.6
Other bonds	**40.4**	250.8
	258.8	476.4
Amounts falling due after more than one year:		
Bank loans	**200.0**	407.0
Other bonds	**2,547.3**	2,205.5
	2,747.3	2,612.5
Total borrowings	**3,006.1**	3,088.9

	2006 £m	2005 £m
Total borrowings are repayable as follows:		
In one year or less	**258.8**	476.4
More than one year, but not more than two years	**–**	207.0
More than two years, but not more than three years	**421.0**	–
More than three years, but not more than four years	**–**	414.0
More than four years, but not more than five years	**247.5**	–
More than five years		
– by instalments	**–**	–
– other than by instalments	**2,078.8**	1,991.5
	3,006.1	3,088.9

The notional amount outstanding of the Company's debt portfolio at 31 March 2006 was £2,894.1m (2005: £3,081.8m).

9. Provisions for liabilities and charges

	Pensions (restated) £m	Deferred taxation (restated) £m	Environmental £m	Other £m	Total £m
At 31 March 2005	27.2	816.3	9.3	12.9	865.7
Prior year adjustment (see below)	(27.2)	8.2	–	–	(19.0)
At 1 April 2005	–	824.5	9.3	12.9	846.7
First time adoption of FRS 26 and FRS 25 (note 1)	–	(3.3)	–	–	(3.3)
At 1 April 2005	–	821.2	9.3	12.9	843.4
Charged to profit and loss account	–	1.3	–	2.4	3.7
Utilised	–	–	(1.5)	(3.0)	(4.5)
Credited to reserves	–	(2.8)	–	–	(2.8)
At 31 March 2006	–	**819.7**	**7.8**	**12.3**	**839.8**

The pensions provision included above at 31 March 2005 was calculated under SSAP 24. The Company has adopted FRS 17 'Retirement Benefits' in full for the year ended 31 March 2006 and comparative figures for 2005 have been restated accordingly. The post-retirement benefits pensions provision calculated according to FRS 17 is included, net of related deferred tax, in note 10.

The environmental provision relates to estimated liabilities relating to uninsured events, principally of an environmental nature. The assessment of this liability is subject to periodic reviews, which may result in the amount being revised. It is currently estimated that substantially all of this provision will be utilised within the next five years. The environmental provision is calculated on an undiscounted basis.

Other provisions includes employer liability provisions of £6.8m (2005: £4.8m) which comprise estimates of liabilities in respect of past events for which no payment date can be identified although it is expected that the liability will be substantially settled over 30 years. Of the remaining balance within other provisions £3.9m (2005: £4.9m) relates to other property commitments estimated to be utilised over the next nine years and £1.6m (2005: £1.7m) relates to a provision created during the previous year to cover protected rights for employees where NGET has an obligation under several deeds of covenant. Other provisions in 2005 included a severance provision of £1.5m utilised in the year.

Deferred taxation

Deferred taxation provided in the financial statements comprises:

	2006 £m	2005 (restated) £m
Accelerated capital allowances	**834.1**	832.0
Other timing differences excluding post-retirement pensions liability	**(14.4)**	(7.5)
	819.7	824.5
Post-retirement pensions liability (note 10)	**(108.6)**	(119.6)
	711.1	704.9

No asset has been recognised for capital losses carried forward. These losses are available to reduce future capital gains. The benefit will only arise if assets giving rise to a capital gain are sold in future periods. The unrecognised deferred tax asset is £1.7m (2005: £1.7m).

There are no other unrecognised deferred tax assets or liabilities.

10. Net post-retirement liability

Substantially all the Company's employees are members of the Electricity Supply Pension Scheme.

The Electricity Supply Pension Scheme provides final salary defined benefits on a funded basis. The assets of the scheme are held in a separate trustee administered fund. The scheme is divided into sections, one of which is the Company's section. The Company's section of the scheme was closed to new entrants on 1 April 2006. It is subject to independent valuations at least every three years, on the basis of which the qualified actuary certifies the rate of employer's contributions 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 under the scheme.

The latest actuarial valuation was carried out by Hewitt Bacon and Woodrow at 31 March 2004. The projected unit method was used and the principal actuarial assumptions adopted were that the annual rate of inflation would be 2.9% and that future real increases in pensionable earnings would be 1.0%. Investments held in respect of pensions before they became payable would average 3.8% real annual rate of return and investments held in respect of pensions after they became payable would average 2.8% real annual rate of return and that pensions would increase at a real annual rate of 0.1%. The aggregate market value of the scheme's assets was £1,110m and the value of the assets represented approximately 80.4% of the actuarial value of benefits due to members calculated on the basis of pensionable earnings and service at 31 March 2004 on an ongoing basis and allowing for projected increases in pensionable earnings. The results of the actuarial valuation carried out at 31 March 2004 showed that, based on long-term financial assumptions, the contribution rate required to meet the future benefit accrual was 19.1% of pensionable earnings (13.1% employers and 6% employees). This contribution rate will be reviewed when the next independent actuarial valuation is carried out, which will be no later than 31 March 2007. The actuarial valuation revealed a pre-tax deficit of £271.5m (£190.1m net of tax) on the basis of the funding assumptions adopted by the actuary.

It has been agreed that no funding of the deficit identified in the 2004 actuarial valuation will need to be provided to the scheme until the outcome of the actuarial valuation at 31 March 2007 is known. At this point, the Company will pay the gross amount of any deficit up to a maximum amount of £67.5m (£47.3m net of tax) into the scheme. Until the 31 March 2007 actuarial valuation has been completed, the Company has arranged for banks to provide the trustees of the National Grid Scheme with letters of credit. The main conditions under which these letters of credit could be drawn relate to events which would imperil the interests of the scheme, such as the Company becoming insolvent or the Company failing to make agreed payments into the fund.

FRS 17 'Retirement Benefits'

The Company has adopted FRS 17 'Retirement Benefits', replacing SSAP 24 'Accounting for Pension Costs', in full for the year ended 31 March 2006 and comparative figures for 2005 have been restated accordingly. Disclosures showing the impact on the Company's profit and loss account and balance sheet, together with other disclosures required by FRS 17, are set out below. The disclosures have been prepared by updating the results of the aforementioned valuation by qualified independent actuaries using the projected unit method of valuation on the basis of the following assumptions:

	2006	2005	2004
Rate of increase in salaries *	**3.9%**	3.9%	3.9%
Rate of increase in pensions in payment	**3.0%**	3.0%	3.0%
Discount rate	**4.9%**	5.4%	5.5%
Rate of increase in RPI	**2.9%**	2.9%	2.9%

* A promotional age related salary scale has also been used.

10. Net post-retirement liability (continued)

An analysis of the assets held in the scheme and the expected rates of return at 31 March 2006, 31 March 2005 and 31 March 2004 were as follows:

	Long term rate of return expected at 31 March 2006	**Value at 31 March 2006 £m**	Long term rate of return expected at 31 March 2005	Value at 31 March 2005 £m	Long term rate of return expected at 31 March 2004	Value at 31 March 2004 £m
Equities	**7.5%**	**814.9**	7.8%	696.6	8.0%	664.5
Gilts	**4.3%**	**293.4**	4.7%	247.3	4.7%	214.4
Bonds	**4.7%**	**100.0**	5.1%	109.4	5.2%	122.3
Property	**6.1%**	**114.4**	6.5%	99.1	6.5%	90.2
Other	**4.0%**	**16.1**	4.0%	11.1	4.0%	14.7
Total market value of assets		**1,338.8**		1,163.5		1,106.1
Present value of scheme liabilities		**(1,700.8)**		(1,562.2)		(1,537.1)
Deficit in the scheme		**(362.0)**		(398.7)		(431.0)
Related deferred tax asset		**108.6**		119.6		129.3
Net pension liability		**(253.4)**		(279.1)		(301.7)

The net pension liability comprises net pension liabilities relating to funded schemes in deficit of £244.2m (2005: £271.0m) and net pension liabilities relating to unfunded schemes in deficit of £9.2m (2005: £8.1m).

The pension deficit has moved during the year ended 31 March as set out below:

	2006 £m	2005 £m
At 1 April	**(398.7)**	(431.0)
Current service cost	**(17.1)**	(15.6)
Net loss on settlements or curtailments	**(1.9)**	(0.1)
Contributions	**14.7**	14.8
Net benefits paid	**0.3**	–
Other finance expense	**(6.5)**	(9.1)
Actuarial losses	**47.2**	42.3
At 31 March	**(362.0)**	(398.7)

The following amounts have been charged/(credited) to the profit and loss account for the year ended 31 March:

	2006 £m	2005 £m
Operating charge		
Current service cost	**17.1**	15.6
Net loss on settlements or curtailments	**1.9**	0.1
Total charge to operating profit	**19.0**	15.7
Other finance (income)/expense		
Expected return on scheme assets	**(76.0)**	(74.1)
Interest on scheme liabilities	**82.5**	83.2
Impact on financial income	**6.5**	9.1
Net profit and loss charge before taxation	**25.5**	24.8

10. Net post-retirement liability (continued)

The following amounts have been recognised directly in equity shareholders' funds:

	2006 £m	2005 £m
Difference between actual and expected return on scheme assets	**170.7**	37.9
Experience losses arising on scheme liabilities	**(11.6)**	(17.2)
Changes in assumptions	**(111.9)**	21.6
Actuarial gains	**47.2**	42.3

History of experience gains and losses:

	2006	2005	2004	2003
Difference between actual and expected return on scheme assets (£m)	**170.7**	37.9	127.0	(316.6)
– percentage of scheme assets	**12.8%**	3.3%	11.5%	(32.7)%
Experience gains arising on scheme liabilities (£m)	**(11.6)**	(17.2)	11.0	7.3
– percentage of present value of scheme liabilities	**(0.7)%**	(1.1)%	0.7%	0.5%
Actuarial gains/(losses) (£m)	**47.2**	42.3	13.0	(369.0)
– percentage of present value of scheme liabilities	**2.8%**	2.8%	0.8%	(26.4)%

11. Share capital

	2006 £m	2005 £m
Authorised:		
2,003,155,130 ordinary shares of £0.10 each	**200.3**	200.3
74,803,600 preference shares of £1 each (2006 – note 6)	**–**	74.8
	200.3	275.1
Allotted, called up and fully paid:		
3,218,870 ordinary shares of £0.10 each	**0.3**	0.3
43,406,000 preference shares of £1 each (2006 – note 6)	**–**	43.4
	0.3	43.7

There has been no movement in ordinary share capital during the year ended 31 March 2006.

The movement in preference shares is explained in note 1.

12. Reconciliation of movement in shareholders' funds

	Share capital £m	Share premium account £m	Capital redemption reserve £m	Special reserve £m	Cash flow hedge reserve £m	Profit and loss account £m	Total shareholders' funds £m
At 1 April 2004							
- as previously stated	43.4	454.1	0.1	28.8	–	358.6	885.0
Prior year adjustment (FRS 17 – note 10)	–	–	–	–	–	(295.9)	(295.9)
Prior year adjustment (FRS 21 – see below)	–	–	–	–	–	350.0	350.0
At 1 April 2004 – as restated	43.4	454.1	0.1	28.8	–	412.7	939.1
Bonus issue of shares	334.9	–	–	(28.8)	–	(306.1)	–
Capital reduction	(334.6)	(454.1)	–	–	–	788.7	–
Actuarial gains	–	–	–	–	–	42.3	42.3
Deferred tax on actuarial gains	–	–	–	–	–	(12.7)	(12.7)
Loss for the year (i)	–	–	–	–	–	(1,085.5)	(1,085.5)
Other movements	–	–	–	–	–	0.1	0.1
At 31 March 2005	43.7	–	0.1	–	–	(160.5)	(116.7)
First time adoption of FRS 26 and FRS 25 (note 1)	(43.4)	–	–	–	(7.5)	3.8	(47.1)
At 1 April 2005	0.3	–	0.1	–	(7.5)	(156.7)	(163.8)
Actuarial gains	–	–	–	–	–	47.2	47.2
Net losses in respect of cash flow hedges	–	–	–	–	(0.5)	–	(0.5)
Share-based payment	–	–	–	–	–	(1.5)	(1.5)
Deferred tax	–	–	–	–	0.1	(11.5)	(11.4)
Profit for the year	–	–	–	–	–	286.8	286.8
At 31 March 2006	**0.3**	**–**	**0.1**	**–**	**(7.9)**	**164.3**	**156.8**

(i) The loss for the year ended 31 March 2005 has increased from the previously stated £741.7m by £350.0m in respect of the the adoption of FRS 21 and decreased by £6.2m in respect of the adoption of FRS 17.

Following the adoption of FRS 21 'Events after the balance sheet date', dividends approved after the balance sheet date are no longer recognised as a liability at the balance sheet date. The proposed dividend of £350.0m at 31 March 2004 has been written back as at that date and charged to profit and loss account in the year ended 31 March 2005 when it was declared. There are no other adjustments in respect of the adoption of FRS 21.

The Company has no non-distributable reserves (2005: £nil).

On 24 March 2005, the Company issued 3,187,000 ordinary shares of £105.08 each at nominal value by way of a bonus issue through the capitalisation of non-distributable reserves, being the special reserve and the non-distributable element of the profit and loss account amounting to £334.9m which was credited to share capital. The Company then underwent a Court approved capital reduction scheme, reducing the nominal value of these shares to 10 pence each, thereby reducing share capital by £334.6m, and also reducing the share premium account to zero. The net result of these transactions was to increase distributable reserves by £788.7m and share capital by £0.3m as compared with the position immediately prior to the issue of shares on 24 March 2005.

13. Commitments and contingencies

Commitments and contingencies for the Company are the same as disclosed in note 28 of the consolidated accounts.

14. Company payroll costs and employees

In respect of the Company, for the year ended 31 March 2006, wages and salaries amounted to £93.8m (2005: £87.7m), social security costs were £9.5m (2005: £8.9m) and other pension costs were £15.3m (2005: £20.7m). Payroll costs capitalised in the year were £27.9m (2005: £29.0m). The average number of employees for the year ended 31 March 2006 was 2,312 (2005: 2,190).

15. Related party transactions

The Company is exempt from disclosing transactions with National Grid plc and other subsidiaries of that company by virtue of the fact that the voting rights of all these companies are held within the National Grid Group.

Under FRS 8 paragraph 3(c), the Company is exempt from disclosing transactions with entities that are part of the Group qualifying as related parties by virtue of the fact that the transactions are disclosed in the ultimate parent company's consolidated accounts.

16. Holding company

The Company's ultimate controlling and parent company is National Grid plc, which owns 100% of the Company's ordinary share capital. The immediate holding company for which consolidated financial statements are prepared is National Grid Holdings Limited. Both companies are incorporated in Great Britain. Copies of their consolidated financial statements can be obtained from their Company Secretary at National Grid plc, 1-3 Strand, London, WC2N 5EH.

National Grid Electricity Transmission plc
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